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No. 07-

IN THE

Supreme Court of the United States

JULIE E. COLLINS AND ROBERT B. RYAN,

Petitioners,

v.

D.R. HORTON, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

BENNETT EVAN COOPER
Counsel of Record
LAWRENCE ALLAN KATZ
STEPTOE & JOHNSON LLP
Collier Center
201 East Washington Street
Suite 1600
Phoenix, Arizona 85004-2382

Attorneys for Petitioners

213143

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

QUESTION PRESENTED

Does the court or the arbitrator determine the preclusive effect of a prior court judgment on the arbitration?

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Julie E. Collins and Robert B. Ryan respectfully petition for a writ of certiorari to review the judgment of the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals is reported at 505 F.3d 874 (App. A, at 1a-21a). The opinion of the district court is reported at 361 F. Supp. 2d 1085 (App. B, at 22a-57a).

JURISDICTION

The judgment of the court of appeals was entered on September 24, 2007. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATEMENT OF THE CASE

This petition raises a long-standing inter-circuit conflict on an important question under the Federal Arbitration Act: Whether the court or the arbitrator determines the preclusive effect on the arbitration of a prior court judgment. Preclusion doctrines reflect fundamental principles of common-law adjudication that command respect for the decisions of courts in conclusively resolving issues and claims. The effect of court decisions should be determined by courts, not arbitrators whose philosophical or economic interests may favor retrying settled matters. This split among the circuits under a statute of nationwide importance should be resolved by this Court.

This is the right case for the Court to decide this issue. Before the arbitration, petitioners Julie E. Collins and Robert B. Ryan sought to have the district court apply offensive non-mutual collateral estoppel to their contract and fraud claims against their former employer; preclusion was based on a jury verdict in the same court in favor of Collins and Ryan's former colleague, who brought identical claims based on the employer's conduct directed toward all three plaintiffs as a group. The district court deferred the issue to the arbitrators, who violated a century of federal precedent by holding that the pending appeal from the jury verdict barred application of collateral estoppel. The arbitrators required relitigation of the contract and fraud issues, and reached a result contrary to what the jury had decided. The district court recognized that the arbitrators had erred by failing to apply collateral estoppel, but it refused to vacate their decision because it felt constrained by the narrow standard of review for arbitrable issues.

On appeal, the Ninth Circuit affirmed, holding that arbitrators should decide the preclusive effect of prior court judgments, subject only to the usual review for "manifest disregard of the law." This conflicted with sister circuits, which have recognized that the application of preclusion based on a prior court judgment is a matter within the primary and plenary authority of the courts, whether they decide the issue before or after the arbitration. This Court should resolve the circuit split and hold that the courts have plenary authority to ensure that the preclusive effects of court judgments are properly enforced, without the constraints imposed by deference to the decisions, however erroneous, of the arbitrators.

I. FACTUAL BACKGROUND

This petition arises from two parallel lawsuits for breach of contract and fraud brought in the United States District Court for the District of Arizona by Julie Collins, Robert Ryan, and Tom Hickcox, who were former employees of defendant D.R. Horton, Inc. ("DRH"), a homebuilder. The three plaintiffs had all been top executives of another homebuilder, Continental Homes Holding Corporation, which DRH acquired through a merger: Hickcox was Continental's President and Chief Executive Officer; Collins was Continental's Chief Financial Officer, Treasurer, and Secretary; and Ryan was Continental's Vice President of Management Information Systems and a member of its board of directors.

During pre-merger negotiations, DRH promised the former company's management group a block of 30,000 shares of DRH stock to be divided among them. This would compensate the management group for the loss of their potential right to accelerate the vesting of a substantial number of unvested Continental stock options if the merger were conducted as a pooling-of-interests transaction, which was DRH's preferred method of merger. DRH President Donald Horton and Executive Vice President Richard Beckwitt made the promise in a face-to-face meeting with several Continental managers, including Collins, Ryan, and Hickcox. After the merger was completed, DRH reneged on the promise, and Collins, Ryan, and Hickcox never received any of the 30,000 shares that DRH had promised to the group.

Collins, Ryan, and Hickcox each sued DRH for breach of contract and fraud. The identity of the issues on both claims flowed inexorably from the fundamentally collective nature of the events and allegations:

- a *single* actor (DRH, through Horton and Beckwitt),
- in a *single* meeting with Continental managers, including Collins, Ryan, and Hickcox,
- entered into a contract, and/or knowingly made a false representation of an intent to pay
- a *single* block of 30,000 shares of DRH stock to be divided among the Continental management *group*,
- where the offer was made to alleviate the *group members' common concern* about their loss of acceleration rights in a pooling-of-interests merger, and
- the offer was intended to induce the *group* to *collectively* support the merger, and
- the group *collectively* relied on the representation by supporting the merger and

- suffered a *collective* harm from DRH's failure to pay the shares of stock *to the group*.

Collins, Ryan, and Hickcox, as members of the group, were thus similarly situated in all respects for purposes of the contract and tort claims based on the promise of 30,000 shares: they heard the promise together; they relied together as members of Continental's top management; and they were harmed together.

II. THE PROCEEDINGS BELOW

A. The Parallel Lawsuits in District Court

On February 22, 1999, Collins and Ryan filed this action against DRH in the District of Arizona. That same day, in the same court, Tom Hickcox filed a similar suit against DRH. The two actions were assigned to different judges. Both actions were litigated for over two years in the district court, through cross-motions for summary judgment, trial memoranda, and motions in limine. Then, after this Court recognized that the Federal Arbitration Act applied to employment contracts, *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2001), DRH moved for the first time to compel arbitration of Collins's and Ryan's claims, but not Hickcox's. Six weeks before the trial date, the district court granted the motion to compel.

A few days after the district court ordered Collins and Ryan to arbitration, the jury in the *Hickcox* case returned its verdict, finding that, among other things, DRH had committed fraud and breach of contract as to

the promise of 30,000 shares of DRH stock. In upholding the verdict, the district court recognized the collective nature of the claims. DRH "was clearly motivated to obtain the enthusiastic support of Continental management for the merger which it had not previously been able to achieve in its first attempt to purchase Continental." ER.229, Ex. D, at 4.[1] DRH "acquired that support, in part, by its promise of 30,000 shares to the Continental managers who would be losing their potential right to accelerate the vesting of their options by accepting the Defendant's offer rather than pursuing negotiations with other suitors." *Id.* As the court concluded, "The representation was material to the Continental managers to whom it was made." *Id.*

The court relied on collective considerations in concluding that the entire Continental management team had actually and reasonably relied on DRH's representations as to the 30,000 shares. As the court found, "the evidence showed that this promise was a turning point in the negotiations between Continental and D.R. Horton. It signaled the beginning of exclusive negotiations, the rejection of negotiations with other suitors, and the unquestioned support by Continental management of the merger." *Id.* at 4-5. "[B]ecause of the promise," the court explained, Continental's management did "not explore[]" any alternative ways to avoid "the loss of the right to accelerate option vesting by the structure of the transaction as a pooling of interest." *Id.*

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[1] In citations to the record before the Ninth Circuit, "ER" refers to Collins and Ryan's Excerpts of Record, and "CR" refers to the Clerk's Record.

Moreover, the court explained, "the jury apparently concluded that the reliance [on the promise] was justifiable because of the significant experience of Horton's executives, Donald Horton and Richard Beckwitt, in mergers and acquisitions and their superior knowledge about the structure of the transaction," which was true vis-à-vis all of the Continental management team, whether collectively or individually. *Id.* at 5.[2]

The district court entered judgment in the *Hickcox* case on April 5, 2002, and it entered an amended judgment on August 20, 2002, after it ruled on the parties' post-trial motions. The parties filed notices of appeal and cross-appeal to the Ninth Circuit.

On May 21, 2002, Collins and Ryan moved for reconsideration by the district court of its order compelling arbitration, arguing that collateral estoppel should be applied based on the *Hickcox* judgment to keep DRH from relitigating issues as to its 30,000-share promise. CR.220. Collins and Ryan later supplemented their motion with the amended judgment entered by the district court in *Hickcox*.

On March 5, 2003, the district court denied Collins and Ryan's motion for reconsideration, holding that the

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[2] In fact, the court cited the pendency of the Collins and Ryan arbitration – "the companion lawsuit involving two other members of the management team that were beneficiaries of the 30,000-share claim" – when it reduced the amount of punitive damages awarded by the jury to Hickcox on the fraud claim, in order to avoid excessive punishment of DRH when Collins and Ryan were later awarded their own fair share of such damages. *Id.* at 7.

issue of collateral estoppel should be decided, at least initially, by the arbitrators. ER.228. The court expressly reminded the parties of judicial precedent establishing the court's retained authority to vacate an arbitration award if arbitrators choose to ignore applicable legal principles. *Id.* at 10-11.

B. The Arbitrators' Refusal to Apply Collateral Estoppel

Collins and Ryan filed a motion with the arbitrators to preclude relitigation of the 30,000-share issues. ER.229, Ex. F. Without even calling for DRH's response, the arbitrators refused to apply collateral estoppel based on the *Hickcox* judgment solely because DRH had filed an appeal from that judgment. They conceded that "the argument for collateral estoppel to at least some issues might be compelling if this were an appealable proceeding in a court of law." ER.229, Ex. G. However, they rejected collateral estoppel because "an appeal is pending in the Hickcox matter, an appeal that we gather will not be resolved until well beyond the projected end of the current proceeding." *Id.* Acknowledging well-established principles, the arbitrators "recognize[d] that the pendency of – and possibility of reversal in – an appeal would not necessarily deprive a judgment of preclusive effect in a collateral proceeding in a court of law." *Id.* Nevertheless, they decided to abandon those principles based on their view that "[p]racticality and fairness suggest a different conclusion in this binding arbitration ... in which the estoppel, if now ordered, cannot later be undone if the Hickcox judgment is later reversed." *Id.* The arbitrators cited no authority for their

newly created exception to the doctrine of collateral estoppel.[3]

As a result, the same 30,000-share issues were retried before the arbitrators. On October 5, 2003, the arbitrators issued their final award, in which they decided – contrary to the *Hickcox* jury and court – that Collins and Ryan had not established that DRH had committed fraud or breach of contract in connection with the promise of 30,000 shares. The arbitrators did not cite any evidence distinguishing Collins' and Ryan's situation from that of Hickcox.

Three days after the arbitrators issued their final award, and one day before the scheduled oral argument in the Ninth Circuit in the *Hickcox* appeal – the same appeal that the arbitrators had used to avoid collateral estoppel – DRH settled Hickcox's claims against it. The appeal and cross-appeal were dismissed, but the district court's judgment was left standing.

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[3] The arbitrators also did not rely on any of the grounds of discretion in applying offensive non-mutual collateral estoppel that this Court recognized in *Parklane Hosiery Co. v. Shore*, 439 U.S. 322 (1979): (i) where the defendant had little incentive to defend the first action vigorously; (ii) where there were multiple inconsistent prior judgments; (iii) where the second action affords the defendant procedural opportunities unavailable in the first action that could readily cause a different result; or (iv) where the plaintiff could easily have joined in the earlier action but adopted a wait-and-see approach.

C. The Courts' Affirmance of the Arbitrators' Decision

Collins and Ryan then moved the district court to vacate the portion of the arbitrators' award relating to the 30,000-share promise because the arbitrators had improperly refused to apply collateral estoppel, and to enter judgment for Collins and Ryan based on collateral estoppel. On March 21, 2005, the district court denied the motion even though it specifically concluded that the arbitrators had committed legal error. App. at 41a-46a, 54a.

The district court conceded that "the rule that a pending appeal does not deprive a judgment of preclusive effect *has no exceptions*," and that "the rule *applies equally to arbitrations* and to proceedings in a court of law." App. at 55a (emphasis added). Indeed, it has been well settled for over a century that "in federal courts . . . the preclusive effects of a lower court judgment cannot be suspended simply by taking an appeal that remains undecided," and this rule applies in situations where "the second judgment has become conclusive even though it rested solely on a judgment that was later reversed." 18A Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and Procedure* § 4433, at 71, 78-79, 88-89 (2d ed. 2002). As leading commentators note, "Despite the manifest risks of resting preclusion on a judgment that is being appealed, the alternative of retrying the common claims, defenses, or issues is even worse," i.e., "the burdens of retrial, the potential for inconsistent results, and the occasionally bizarre problems of achieving repose and finality that may arise." *Id.* at 94.

Further, the district court found "that general principles of fairness and practicality are not sufficient grounds to dispense with collateral estoppel under federal law." App. at 55a. It held that "[t]he arbitrators were therefore not free to refuse to give the *Hickcox* judgment preclusive effect on the basis of their overriding sense of fairness and practicality," App. at 51a.

Nevertheless, the district court declined to vacate the award because it reviewed the application of collateral estoppel under the standard of "manifest disregard of the law," rather than do novo. Applying a "mens rea" requirement, the court held, "Although the arbitrators committed an error of law, the Court cannot conclude that the arbitrators understood they were acting in error. It therefore cannot find that the arbitrators acted in 'manifest disregard of the law.'" App. at 56a.

On appeal, Collins and Ryan argued that the courts, not the arbitrators, should ultimately determine the application of preclusion doctrines and that the manifest-disregard standard should not apply.[4] Alternatively, Collins and Ryan argued that the arbitrators had engaged in manifest disregard. The Ninth Circuit rejected both arguments. First, the court held that while "'[a]rbitrators are not free to ignore the preclusive effect of prior judgments under the doctrines of res judicata

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[4] *See* Opening Br. at 12-13, 29-30; Reply Brief at 23; Oral Argument audio file, *available at* http://www.ca9.uscourts.gov/ca9/media.nsf/Media%20Search?OpenForm&Seq=2 (last visited Dec. 24, 2007).

and collateral estoppel,'" nevertheless "arbitrators are entitled to determine in the first instance whether the prerequisites for collateral estoppel are satisfied." App. at 17a (quotation omitted). In addition, the court held that "arbitrators possess the same broad discretion possessed by district courts to determine when to apply offensive non-mutual collateral estoppel" under *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, (1979). App. at 11a-12a; *see id.* at 17a. Unlike the district court, the Ninth Circuit expressly declined to resolve whether the arbitrators had abused their discretion, conducting instead limited review under the manifest-disregard standard. App. at 21a. The court concluded that the arbitrators did not manifestly disregard the law because "no *binding* precedent existed" on the application of offensive non-mutual collateral estoppel in a subsequent arbitration while the prior judgment was on appeal. *Id.* (emphasis added).

REASONS FOR GRANTING THE PETITION

I. THE NINTH CIRCUIT HAS EXPANDED A CONFLICT AMONG THE CIRCUITS AS TO WHETHER THE COURT OR THE ARBITRATOR DETERMINES THE PRECLUSIVE EFFECT OF A PRIOR COURT JUDGMENT.

In its opinion below, the Ninth Circuit widened an existing split among the circuits as to whether the court or the arbitrator determines the preclusive effect of a prior court judgment on an arbitration proceeding. The Ninth Circuit held that preclusion is to be treated like any other arbitrable issue: "arbitrators are entitled to

determine in the first instance whether the prerequisites for collateral estoppel are satisfied," App. at 17a, and the subsequent judicial review is under the narrow manifest-disregard standard, *id.* at 21a.

The Ninth Circuit thus squarely answered the question that a prior panel of that court had explored at greater length in *Chiron Corp. v. Ortho Diagnostic Systems, Inc.*, 207 F.3d 1126 (9th Cir. 2000). (Indeed, the panels overlapped in membership.) In *Chiron*, the Ninth Circuit acknowledged authority from other circuits recognizing that the preclusive effect of a federal judgment was ultimately for the court to decide, not the arbitrator. *Id.* at 1134. But in *Chiron*, the precise issue was the preclusive effect of a *prior arbitration*, and the Ninth Circuit distinguished that context from one in which the prior judgment arose from *judicial* proceedings rather than an arbitration. In doing so, it acknowledged "the presumption that the court issuing the original decision is best equipped to determine ... what is or is not precluded by that decision." *Id.* The Ninth Circuit has now granted arbitrators the identical power to determine preclusion even though the prior judgment was that of the same federal court and based on a jury verdict. App. at 17a (citing *Aircraft Braking Systems Corp. v. Local 856, Int'l Union*, 97 F.3d 155, 159 (6th Cir. 1996) (recognizing that arbitrators "generally are entitled to determine in the first instance whether to give the prior judicial determination preclusive effect")). In doing so, the court joined the Second and Eleventh Circuits in holding that the preclusive effect of a prior court judgment is itself arbitrable. *United States Fire Ins. Co. v. Nat'l Gypsum Co.*, 101 F.3d 813, 816-17 (2d Cir. 1996); *Klay v. United Healthgroup, Inc.*, 376 F.3d 1092, 1109 (11th Cir. 2004).

The Third, Fifth, and Eighth Circuits, however, along with district courts in other circuits and some state courts, have held that courts' consideration of preclusion issues is plenary, not limited by the usual manifest-disregard standard. Some circuits have held that the courts should decide the issue in the first instance, while others have permitted arbitrators to consider the issue first, subject to full court review. *See, e.g., John Hancock Mut. Life Ins. Co. v. Olick*, 151 F.3d 132, 139 (3d Cir. 1998) (district court should determine res judicata effect of judgment at time of contested arbitral demand); *Tel. Workers Union, Local 827 v. N.J. Bell Tel. Co.*, 584 F.2d 31, 33 (3d Cir. 1978) (affirming district court's rejection of arbitrators' decision based on collateral estoppel effect of prior judicial decision); *Miller Brewing Co. v. Fort Worth Distrib. Co.*, 781 F.2d 494, 499 (5th Cir. 1986) (parties should be barred from seeking relief from an arbitration panel if res judicata principles would bar relief in federal court); *John Morrell & Co. v. Local Union 304A, UFCW*, 913 F.2d 544, 562-63 (8th Cir. 1990) (affirming district court's vacating of arbitration award based on collateral estoppel effect of prior jury determination of same issue); *Ewart v. Y & A Group, Inc. (In re Y & A Group Secs. Litig.)*, 38 F.3d 380, 382-83 (8th Cir. 1994) (district court could enjoin arbitration of previously determined issues based on collateral estoppel because "[t]he district court, and not the arbitration panel, is the best interpreter of its own judgment"); *Leon C. Baker, P.C. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 821 So. 2d 158, 164 (Ala. 2001) (holding that the trial court, not the arbitrator, was the proper forum for resolving collateral estoppel). As one court summarized, "However limited our jurisdiction [to review arbitration awards] is, we have the power to

determine if the arbitral panel was precluded from its action by our [prior] decision. . . ." *Am. Train Dispatchers Ass'n v. Burlington N.R.R. Co.*, 784 F. Supp. 899, 903 (D.D.C. 1992). "[C]ourts have the right of plenary review when asked to determine the preclusive effects of a federal judgment on relitigation of the same issues in an arbitral forum." *Id.*

In 2001, the Alabama Supreme Court comprehensively surveyed the precedent nationally on "[t]he question of *who decides* whether the arbitration of a previously *litigated* issue is collaterally estopped," and it found that the "courts have reached divergent conclusions." *Leon C. Baker, P.C.*, 821 So. 2d at 163. Since this Court's last decision regarding the respective roles of courts and arbitrators, *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003), that divergence has not been resolved. Some courts have recognized that the preclusive effect of a prior court judgment is to be determined by the court, not the arbitrator. *See, e.g.*, *Duhaime v. John Hancock Mut. Life Ins. Co.*, 200 Fed. Appx. 6, 8 (1st Cir. 2006) (recognizing that the "preclusive effect of [a] prior court judgment" is among the "disputes that have generally been held to be matters for the court"); *Drag v. SouthTrust Bank*, No. 3:04CV319-H, 2005 WL 1883241, at *6 (W.D.N.C. Aug. 4, 2005) (enjoining arbitration based on res judicata effects of prior judgment); *W. Dow Ham III Corp. v. Millenium Income* Fund, __ S.W.3d __, 2007 WL 2005071, at 8 (Tex. Ct. App. July 12, 2007) (noting at headnote 13 that court may determine res judicata effect of prior judgment); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Benjamin*, 766 N.Y.S.2d 1, 6 (App. Div. 2003) ("determining the preclusive effect of court judgments

on subsequent arbitrations is another subject 'so interlaced with strong public policy considerations that [it must be] placed beyond the reach of the arbitrators' discretion'" (quotation omitted)).

On the other hand, other courts have held that the preclusive effect of a prior court judgment is to be decided by the arbitrator. *See Klay*, 376 F.3d at 1109; *Zurich Am. Ins. Co. v. Watts Indus., Inc.*, 415 F. Supp. 2d 887, 890 (N.D. Ill. 2006). It therefore remains true that state and "federal courts have reached seemingly disparate and conflicting conclusions" on the issue. Jarrod Wong, *Court or Arbitrator – Who Decides Whether Res Judicata Bars Subsequent Arbitration Under the Federal Arbitration Act?*, 46 Santa Clara L. Rev. 49, 58-59 (2005).

In affirming the primary role of the courts in determining the preclusive effect of a prior court judgment on an arbitration, the Third Circuit properly reconciled critical principles of preclusion with the federal policy favoring arbitration. "When a federal court is presented with the contention that a prior federal judgment determined issues now sought to be relitigated in an arbitral forum [the court] must *first* determine the effect of the judgment." *Tel. Workers Union*, 584 F.2d at 33 (emphasis added). Before then, the court noted, the "federal policy favoring [arbitration] clauses . . . does not come into play." *Id.* Contrary to these principles, the Ninth Circuit placed the issue of preclusion in the hands of the arbitrators, subject to the same limited, deferential judicial review given to ordinary arbitrable issues. The Ninth Circuit's ruling cannot be reconciled with the rulings of these other circuits.

II. THIS CASE PROPERLY RAISES THE CRITICAL ISSUE OF WHO SHOULD DECIDE A JUDGMENT'S PRECLUSIVE EFFECT.

This case raises this circuit split in the best possible manner. First, Collins and Ryan raised the issue of who should determine the collateral estoppel issue early and repeatedly. Immediately after the *Hickcox* verdict was returned, they sought reconsideration of the district court's order referring the case to arbitration on the ground that the court should decide the issue-preclusive effect of that verdict on Collins' and Ryan's own claims. After the court declined to decide the issue but left open the possibility of review after the arbitration, Collins and Ryan presented their preclusion arguments to the arbitration panel. After the arbitrators refused to apply collateral estoppel and reached a conclusion diametrically opposed to that of the *Hickcox* jury, Collins and Ryan again sought to have the district court reexamine the issue. On appeal, Collins and Ryan again pressed for the Ninth Circuit's plenary review of the preclusion issue.

Second, whether the court or arbitrators decide the preclusion issue determines the outcome of this case. The arbitrators conceded that "the argument for collateral estoppel to at least some issues might be *compelling* if this were an appealable proceeding in a court of law." ER.229, Ex. G (emphasis added).) They rejected issue preclusion solely because "an appeal is pending in the Hickcox matter, an appeal that we gather will not be resolved until well beyond the projected end of the current proceeding." *Id.* On the other hand, "the district court . . . [held] that the arbitrators erred

by not giving preclusive effect to Hickcox's judgment." App. at 8a; *see id.* at 56a The district court recognized that "the rule that a pending appeal does not deprive a judgment of preclusive effect *has no exceptions*," and that "the rule *applies equally to arbitrations* and to proceedings in a court of law." App. at 55a (emphasis added). Despite finding error, the court upheld the arbitrators' decision solely because it was applying the manifest-disregard standard, rather than deciding the issue itself by conducting a plenary review. App. at 54a. On appeal, the Ninth Circuit affirmed on the basis of the limited scope of manifest-disregard review, without even deciding whether the arbitrators' decision had been incorrect. App. at 21a. The circuit held that the discretion under *Parklane Hosiery* belonged to the *arbitrators* both in the first instance and ultimately, not the district court. App. at 17a. Thus, the outcome was determined by the choice of decision maker.

III. THIS CASE PRESENTS AN ISSUE WITH IMPORTANT NATIONAL IMPLICATIONS.

This circuit split implicates the relationship between courts and arbitration panels in the context of preclusion doctrines that are "[a] fundamental precept of common-law adjudication." *Montana v. United States*, 440 U.S. 147, 153 (1979). As this Court has emphasized, "a fundamental precept of common-law adjudication is that an issue once determined by a competent court is conclusive." *Arizona v. California*, 460 U.S. 605, 619 (1983). "Collateral estoppel, like the related doctrine of res judicata, has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial

economy by preventing needless litigation." *Parklane Hosiery*, 439 U.S. at 326. "Application of both doctrines is central to the purpose for which civil courts have been established, the conclusive resolution of disputes within their jurisdictions." *Montana*, 440 U.S. at 153.

The conflict raised here presents what is essentially a corollary of the principle recognized by this Court that, with a few exceptions, the courts have "the primary power to decide arbitrability" of a dispute, not the arbitrator. *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995); *see also Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1985) ("[T]he first task of a court asked to compel arbitration of a dispute is to determine whether the parties agreed to arbitrate that dispute."). When a court decides an issue in a manner that raises collateral estoppel, the conclusive judicial determination removes the issue from range of issues that are still litigable or arbitrable. Like the absence of consent of the parties to arbitration, a final judicial decision is a limitation on the scope of arbitrability that is extrinsic to the arbitration procedures themselves.

Moreover, the preclusive effect of a prior *judicial* decision is "the kind of narrow circumstance where contracting parties would likely have expected a court to have decided the gateway matter." *Howsam v. DeanWitter Reynolds, Inc.*, 537 U.S. 79, 83-84 (2002). It is not a mere procedural question that grows out of

the dispute. *See id.* at 84.[5] The preclusive effects of *judges'* determinations are quintessentially questions that "concern ... judicial procedures" and that parties would expect *judges* to decide. *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. at 452-53 (plurality). Just as this Court held that NASD arbitrators were "comparatively more expert about the meaning of their own [time-limit] rule" and "comparatively better able to interpret and to apply it," *Howsam*, 537 U.S. at 85, courts are more expert about the meaning of judgments and better able to apply them to other disputes – particularly where, as here, the courts are applying their *own* prior judgments.

Like decisions as to substantive arbitrability, decisions on relitigation in the arbitration of judicially determined issues or claims should be made by the courts. *See First Options*, 514 U.S. at 944 (recognizing that "the law reverses the presumption" of arbitrability when the issue is who decides arbitrability, rather than the merits of the dispute). Like arbitrability, the issue of preclusion may reach the courts either before the arbitration or after the award. The court's exercise of the plenary power to decide the issue should be the

[5] *Cf. Federated Dept. Stores, Inc. v. Moitie*, 452 U.S. 394, 401(1981) (reiterating that "'res judicata is not a mere matter of practice or procedure inherited from a more technical time than ours,'" but is instead "'a rule of fundamental and substantial justice'" (quotation omitted)); *Baker Elec. Co-op., Inc. v. Chaske*, 28 F.3d 1466, 1475 (8th Cir. 1994) ("Res judicata and collateral estoppel are issues of substantive law. . . ."); *Lynch v. Merrell-National Labs.*, 830 F.2d 1190, 1192 (1st Cir. 1987) ("The law on collateral estoppel is as substantive in its effect as the law of contracts or torts.").

same pre-arbitration or post-award. *See generally* 2 Ian R. Macneil et al., *Federal Arbitration Law* § 15.1.4, at 15:5 (Supp. 1999) ("*First Options* was a post-award case, but its principles apply to pre-award situations, such as proceedings to compel arbitration.").

This dispute over who decides preclusion highlights a broader struggle between judicial and arbitral systems. Arbitrators have institutional or philosophical reasons to reject the preclusive effect of prior judgments and decide the issues and claims anew. They may believe that they are simply smarter, better educated, or endowed with greater industry expertise than jurors, or less constrained by resource or time limitations and procedural niceties than judges, and thus better suited and equipped to decide issues accurately, fairly, and dispassionately. "Some arbitrators and mediators . . . believe that virtually every dispute can be resolved by ADR and that a mediated or arbitrated resolution is almost always vastly superior to a litigated one. It is also good for their business." Scott Atlas & Nancy Atlas, *Potential ADR Backlash*, 10 No. 4 Disp. Resol. Mag. 14, 15-16 (2004); *see also* Chris Guthrie, *Misjudging*, 7 Nev. L.J. 420, 454-55 (Spring 2007) (arguing that "arbitrators often offer the potential advantage of subject-matter expertise" that "is seldom the case in jury trials," and that "arbitrators, by virtue of their specialized subject-matter knowledge, might be better able than general jurisdiction judges to make accurate decisions").

Citing their concern that, for these reasons, arbitrators may improperly decline to apply preclusion doctrines, courts have recognized the ultimate authority of courts to determine whether such doctrines apply.

See, e.g., *John Morrell*, 913 F.2d at 562 (court may vacate an arbitration award if the arbitrator's decision on issue preclusion disregards judicial precedent in favor of his "own brand of industrial justice"); *Hudson-Berlind Corp. v. Local 807, IBT*, 597 F. Supp. 1282, 1285 (E.D.N.Y. 1984) (warning of the danger of taking from courts the power to determine the preclusive effect of a judgment and giving that power to an arbitrator "who might not be as respectful of such judgments as courts would be").

The threat that professional hubris poses to the fair application of preclusion doctrines is compounded by the fact that arbitrators are not salaried judicial officers but instead are compensated based on the scope and duration of their arbitral efforts. The disinclination of arbitrators to

> terminate a dispute as a result of a pre-trial motion, such as a motion to dismiss or motion for summary judgment . . . may arise from a desire to hear the parties out, but it also might be influenced by the arbitrators' self-interest in extending their ability to bill the parties for their services.

Henry S. Noyes, *If You (Re)Build It, They Will Come: Contracts to Remake the Rules of Litigation in Arbitration's Image*, 30 Harv. J.L. & Pub. Pol'y 579, 588 (2007); *see* Mark Berger, *Arbitration and Arbitrability: Toward an Expectation Model*, 56 Baylor L. Rev. 753, 787-88 (Fall 2004) (noting "no documented support" for the proposition that "arbitrators will put their own interests ahead of their responsibilities").

The reluctance of arbitrators to apply preclusion doctrines ultimately undermines the utility of arbitration as a solution in our legal system. Arbitration is advanced as a means of resolving disputes more quickly and less expensively, and it has been criticized for failing to meet that goal. *See* Noyes, *supra*, at 584-89. The failure to apply preclusion doctrines will make arbitration an even more time-consuming and costly form of dispute resolution and make parties less willing to agree to it in the first place. "The doctrine of res judicata and its cousin collateral estoppel have probably done more to prevent useless and wasteful litigation that arbitration ever could." *Miller Brewing*, 781 F.2d at 497 n.3 (internal citation omitted).

The Court should ensure that arbitration remains a streamlined process. Allowing extrajudicial actors to determine the force and effect of judicial determinations should be unacceptable, particularly where, as here, the court involved in the second suit is the same one that issued the prior judgment. Decisions as to arbitrability are generally left safely in the hands of the courts. While procedural requirements are generally left to the arbitrators, those issues do not raise the direct conflict with judicial authority that is created when arbitrators decide with effective finality whether they are bound by prior judicial determinations of issues and claims. Such issues as the force and effect of court judgments should be decided by courts, not arbitrators. Without plenary review by the courts of those decisions, preclusion doctrines cannot fulfill their fundamental role in our legal system.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

BENNETT EVAN COOPER
Counsel of Record
LAWRENCE ALLAN KATZ
STEPTOE & JOHNSON LLP
Collier Center
201 East Washington Street
Suite 1600
Phoenix, Arizona 85004-2382

Attorneys for Petitioners

APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT FILED SEPTEMBER 24, 2007

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 05-15737

JULIE E. COLLINS; ROBERT B. RYAN, individuals,

Plaintiffs-Appellants,

v.

D.R. HORTON, INC., a Delaware corporation,

Defendant-Appellee.

Argued and Submitted April 17, 2007
Filed Sept. 24, 2007

Before: DOROTHY W. NELSON, CONSUELO M. CALLAHAN, and CARLOS T. BEA, Circuit Judges.

BEA, Circuit Judge:

Julie E. Collins and Robert B. Ryan ("Appellants") appeal the district court's denial of their motion to vacate an arbitration award. Appellants contend their motion should have been granted because the arbitrators manifestly disregarded the law when deciding not to

apply offensive non-mutual collateral estoppel[1] because judicial review of an arbitration award under the Federal Arbitration Act ("FAA") is more limited than judicial review of a district court judgment. We hold the arbitrators did not manifestly disregard the law because no "well defined, explicit, and clearly applicable" law existed to be disregarded. *Carter v. Health Net of Cal., Inc.*, 374 F.3d 830, 838 (9th Cir.2004). Accordingly, we affirm.

I.

Continental Homes Holding Corporation ("Continental") was a homebuilding and mortgage business headquartered in Arizona. In 1996, D.R. Horton, Inc. ("Horton"), a homebuilding company with operations in several states, expressed an interest in merging with Continental. Although Continental initially rebuffed Horton's merger proposals, Horton and Continental negotiated and entered into a merger agreement in 1997.

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1. "Offensive non-mutual collateral estoppel is a version of the doctrine [of collateral estoppel] that arises when a plaintiff seeks to estop a defendant from relitigating an issue which the defendant previously litigated and lost against another plaintiff." *Appling v. State Farm Mut. Auto. Ins. Co.*, 340 F.3d 769, 775 (9th Cir.2003) (citing *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326, 99 S.Ct. 645, 58 L.Ed.2d 552 (1979) ("Defensive use occurs when a defendant seeks to prevent a plaintiff from asserting a claim the plaintiff has previously litigated and lost against another defendant.")).

Appendix A

To make itself a more attractive merger partner, Continental entered into employment contracts with key employees designed to induce them to stay on with the merged company for at least that period of time sufficient to accomplish the merger and the related combination of operations. Among those Continental employees who entered into such employment contracts were Appellants and W. Thomas Hickcox ("Hickcox").[2] The employment contracts provided for severance packages if Appellants or Hickcox were terminated without cause or resigned "for good reason," such as a significant reduction in responsibility.

During merger negotiations, an issue arose concerning whether Continental employees would be able to accelerate vesting of their unvested Continental stock options prior to or as part of the merger. Both Appellants and Hickcox contend Horton overcame this issue by verbally promising to give 30,000 shares of Horton stock to be divided by the group of Continental managers holding unvested Continental stock options, including Appellants and Hickcox.

The merger between Continental and Horton became effective in April 1998. Shortly after the merger, Horton terminated Hickcox without cause and Appellants resigned pursuant to the "for good reason" provisions in their employment contracts. Horton failed

2. Collins was Continental's Chief Financial Officer, Treasurer, and Secretary. Ryan was the Vice President of Management Information Systems and a member of the Board of Directors. Hickcox was Continental's Chief Executive Officer.

to honor the severance packages called for under both Appellants' and Hickcox's employment contracts. Appellants and Hickcox also contend Horton failed to honor its promise to give Continental's managers holding unvested Continental stock options 30,000 shares of Horton stock.

On February 22, 1999, Hickcox alone filed a diversity action against Horton in district court, alleging state law claims for breach of contract, failure to pay wages, promissory estoppel, and fraud. The same day, Appellants jointly filed a separate and distinct diversity action against Horton in the same district court, also alleging breach of contract, failure to pay wages, promissory estoppel, and fraud. Appellants and Hickcox made nearly identical breach of contract and fraud claims related to Horton's 30,000 share promise.

On May 14, 1999, pursuant to a mandatory arbitration clause in Hickcox's employment contract, Horton moved to dismiss Hickcox's case and compel arbitration. At the time, our precedent held that the FAA did not apply to employment contracts and, therefore, compulsory arbitration clauses in employment contracts were unenforceable.[3] *See Craft v. Campbell Soup Co.*, 177

3. In relevant part, the FAA states:

> A written provision in any maritime transaction or a *contract evidencing a transaction involving commerce* to settle by arbitration a controversy thereafter arising out of such contract or transaction,

(Cont'd)

F.3d 1083, 1093 (9th Cir.1999). The district court, therefore, denied Horton's motion to compel arbitration in Hickcox's case.

After discovery and unsuccessful summary judgment motions, Horton moved to consolidate Appellants' and Hickcox's cases for trial on the basis that both cases involved Horton's alleged 30,000 share promise. The district court denied the motion because the difference between Appellants' and Hickcox's employment contract claims, i.e., resignation for good cause versus termination without cause, outweighed the benefit of consolidation. Hickcox's and Appellants' trials were set for March 12, 2002 and May 14, 2002,

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> or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 2 (emphasis added).

In *Craft v. Campbell Soup Co.*, 177 F.3d 1083 (9th Cir.1999), we held that the FAA did not apply to employment contracts because an employment contract is not a "contract evidencing a transaction involving interstate commerce." The Supreme Court overruled *Craft*, holding the phrase "contract evidencing a transaction involving interstate commerce" is not limited to commercial contracts and, therefore, includes employment contracts. *See Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 114, 121 S.Ct. 1302, 149 L.Ed.2d 234 (2001).

respectively. On March 28, 2002, a jury found Horton liable for breaching the severance package provisions of Hickcox's employment contract and fraud as to the making of the 30,000 share promise. The jury awarded Hickcox $87,500 in compensatory damages on the breach of contract claim, $87,000 in damages on the fraud claim, and $4,100,000 in punitive damages, which the district court ordered remitted to $1,000,000 in punitive damages.

Prior to the start of Appellants' trial, the district court granted a motion by Horton to compel arbitration of Appellants' case because the Supreme Court had reversed our precedent and held that arbitration clauses in employment contracts are enforceable under the FAA. *See Circuit City Stores*, 532 U.S. at 114, 121 S.Ct. 1302.

Appellants' claims were arbitrated before a panel of three arbitrators. Appellants moved for summary judgment as to their 30,000 share claims, contending that offensive non-mutual collateral estoppel based on the judgment in Hickcox's case barred Horton from relitigating their 30,000 share claims. The arbitration panel denied Appellants' motion for summary judgment:

Although the argument for collateral estoppel to at least some issues might be compelling if this were an appealable proceeding in a court of law, the arbitrators conclude that collateral estoppel should *not* be applied in this binding arbitration. The reason is that an appeal is pending in the Hickcox matter, an appeal that we gather will not be resolved until well beyond the

projected end of the current proceedings. We recognize that the pendency of—and possibility of reversal in—an appeal would not necessarily deprive a judgment of preclusive effect in a collateral proceeding in a court of law. There, the availability of an appeal of the second proceeding would permit the estoppel to be undone and the second judgment to be set aside if the prior judgment were ultimately reversed. Practicality and fairness suggest a different conclusion in this binding arbitration, however, in which the estoppel, if now ordered, cannot later be undone if the Hickcox judgment is later reversed. Such, in any event, is our understanding, and on the basis of that understanding we . . . deny [ ] the motion of Plaintiffs . . . that collateral estoppel be attributed in this matter to issues resolved against [Horton] . . . in the Hickcox case.

Thereafter, the arbitrators found for Appellants on their breach of employment contract claims. The arbitrators, however, found for Horton on Appellants' claims arising from Horton's alleged 30,000 share promise.

Pursuant to 9 U.S.C. § 9,[4] Appellants filed in district court an application to vacate that portion of the

4. In relevant part, § 9 of the FAA states:

> If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year

(Cont'd)

arbitration award holding Appellants had "not established, either on grounds of breach of contract, promissory estoppel, or fraud, that Horton made an enforceable promise" to give 30,000 shares of Horton stock to Continental managers holding unvested Continental stock options. Appellants' application to vacate the arbitration award contended that the arbitrators displayed a manifest disregard for the law when deciding not to apply offensive non-mutual collateral estoppel to bar Horton from relitigating whether Horton made an enforceable 30,000 share promise.

The district court denied Appellants' application to vacate the arbitration award, holding that the arbitrators erred by not giving preclusive effect to Hickcox's judgment but that this error did not rise to the level of a manifest disregard for the law.

(Cont'd)

> after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title. If no court is specified in the agreement of the parties, then such application may be made to the United States court in and for the district within which such award was made.

9 U.S.C. § 9.

II.

We review *de novo* the district court's denial of Appellants' motion to vacate the arbitration award. *See Woods v. Saturn Distrib. Corp.*, 78 F.3d 424, 427 (9th Cir.1996). Our review, however, is necessarily limited: "Broad judicial review of arbitration decisions could well jeopardize the very benefits of arbitration, [i.e., speed and informality,] rendering informal arbitration merely a prelude to a more cumbersome and time-consuming judicial review process." *Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 998 (9th Cir.2003) (en banc).

Under 9 U.S.C. § 10, a district court may vacate an arbitration award only:

> (1) where the award was procured by corruption, fraud or undue means; (2) where there was evident partiality or corruption on the part of the arbitrators; (3) where the arbitrators were guilty of misbehavior by which the rights of any party have been prejudiced; or (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

9 U.S.C. § 10. Although § 10 does not sanction judicial review of the merits of arbitration awards, we have adopted a narrow "manifest disregard of the law"

exception under which a procedurally proper arbitration award may be vacated. This standard was first articulated in dicta in *Wilko v. Swan*, 346 U.S. 427, 436-37, 74 S.Ct. 182, 98 L.Ed. 168 (1953) ("[T]he interpretations of the law by the arbitrators *in contrast to manifest disregard*, are not subject, in the federal courts, to judicial review for error in interpretation."(emphasis added)). The manifest disregard exception requires "something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand and apply the law." *San Martine Compania De Navegacion, S.A. v. Saguenay Terminals Ltd.*, 293 F.2d 796, 801 (9th Cir.1961). Accordingly, we may not reverse an arbitration award even in the face of an erroneous interpretation of the law. *See A.G. Edwards v. McCollough*, 967 F.2d 1401, 1403 (9th Cir.1992). Rather, to demonstrate manifest disregard, the moving party must show that the arbitrator "understood and correctly state[d] the law, but proceed[ed] to disregard the same." *San Martine Compania De Navegacion*, 293 F.2d at 801.

In short, "federal courts of appeals have repeatedly held, 'manifest disregard of the law' means something more than just an error in the law or a failure on the part of the arbitrators to understand or apply the law. It must be clear from the record that the arbitrators recognized the applicable law and then ignored it. As such, mere allegations of error are insufficient." *Carter*, 374 F.3d at 838 (internal citations, quotation marks, and alterations omitted). Moreover, to rise to the level of manifest disregard "[t]he governing law alleged to have

been ignored by the arbitrators must be *well defined, explicit, and clearly applicable."Id.* (emphasis added).

III.

We have "not specifically addressed whether arbitrators are bound by prior federal court decisions under the doctrines of collateral estoppel and/or res judicata[.]" *Collins v. Horton*, 361 F.Supp.2d 1085, 1097 (D.Ariz.2005). Other circuits, however, have held that where the prerequisites for collateral estoppel are satisfied arbitrators must give preclusive effect to prior federal judgments. *See, e.g., Aircraft Braking Sys. Corp. v. Local 856*, 97 F.3d 155, 159 (6th Cir.1996); *Miller v. Runyon*, 77 F.3d 189, 193 (7th Cir.1996); *John Morrell & Co. v. Local Union 304A*, 913 F.2d 544 (8th Cir.1990). We agree: "Arbitrators are not free to ignore the preclusive effect of prior judgments under the doctrines of res judicata and collateral estoppel, although they generally are entitled to determine in the first instance whether to give the prior judicial determination preclusive effect." *Aircraft Braking Sys. Corp.*, 97 F.3d at 159;*see also Miller Brewing Co. v. Fort Worth Distrib. Co.*, 781 F.2d 494, 499 (5th Cir.1986) (reasoning that parties should be barred from seeking relief from an arbitration panel if res judicata principles would bar relief in federal court because an arbitration award involves the entry of judgment by a court).

These circuits, however, have not addressed the question presented here, i.e., whether arbitrators possess the same broad discretion possessed by district

courts to determine when to apply offensive non-mutual collateral estoppel. As noted above, "[o]ffensive non-mutual collateral estoppel is a version of the doctrine [of collateral estoppel] that arises when a plaintiff seeks to estop a defendant from relitigating an issue which the defendant previously litigated and lost against another plaintiff." *Appling*, 340 F.3d at 775 (citing *Parklane Hosiery Co.*, 439 U.S. at 326, 99 S.Ct. 645). The Supreme Court has explained why district courts possess broad discretion in the application of offensive non-mutual collateral estoppel:

> Collateral estoppel, like the related doctrine of res judicata,[5] has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation. Until relatively recently, however, the scope of collateral estoppel was limited by the doctrine of mutuality of parties. Under this mutuality doctrine, neither party could use a prior judgment as an estoppel against the

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5. "Under the doctrine of res judicata, a judgment on the merits in a prior suit bars a second suit involving the same parties or their privies based on the same cause of action. Under the doctrine of collateral estoppel, on the other hand, the second action is upon a different cause of action and the judgment in the prior suit precludes relitigation of issues actually litigated and necessary to the outcome of the first action." *Parklane Hosiery Co., Inc.*, 439 U.S. at 326-27 n. 5, 99 S.Ct. 645 (citations omitted).

other unless both parties were bound by the judgment. Based on the premise that it is somehow unfair to allow a party to use a prior judgment when he himself would not be so bound, the mutuality requirement provided a party who had litigated and lost in a previous action an opportunity to relitigate identical issues with new parties.[6]

By failing to recognize the obvious difference in position between a party who has never litigated an issue and one who has fully litigated and lost, the mutuality requirement was criticized almost from its inception. Recognizing the validity of this criticism, the Court in *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation*, [402 U.S. 313, 329, 91 S.Ct. 1434, 28 L.Ed.2d 788 (1971)], abandoned the mutuality requirement, at least in cases where a patentee seeks to relitigate the validity of a patent after a federal court in a previous lawsuit has already declared it invalid.

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6. "It is a violation of due process for a judgment to be binding on a litigant who was not a party or a privy and therefore has never had an opportunity to be heard." *Parklane Hosiery Co., Inc.*, 439 U.S. at 327, 99 S.Ct. 645 (citations omitted).

Appendix A

The *Blonder-Tongue* case involved defensive use of collateral estoppel—a plaintiff was estopped from asserting a claim that the plaintiff had previously litigated and lost against another defendant. The present case, by contrast, involves offensive use of collateral estoppel—a plaintiff is seeking to estop a defendant from relitigating the issues which the defendant previously litigated and lost against another plaintiff. In both the offensive and defensive use situations, the party against whom estoppel is asserted has litigated and lost in an earlier action. Nevertheless, several reasons have been advanced why the two situations should be treated differently.

First, offensive use of collateral estoppel does not promote judicial economy in the same manner as defensive use does. Defensive use of collateral estoppel precludes a plaintiff from relitigating identical issues by merely switching adversaries. Thus defensive collateral estoppel gives a plaintiff a strong incentive to join all potential defendants in the first action if possible. Offensive use of collateral estoppel, on the other hand, creates precisely the opposite incentive. Since a plaintiff will be able to rely on a previous judgment against a defendant but will not be bound by that judgment if the defendant wins, the plaintiff has every incentive to adopt a "wait and see" attitude, in the hope that the

first action by another plaintiff will result in a favorable judgment. Thus offensive use of collateral estoppel will likely increase rather than decrease the total amount of litigation, since potential plaintiffs will have everything to gain and nothing to lose by not intervening in the first action.

A second argument against offensive use of collateral estoppel is that it may be unfair to a defendant. If a defendant in the first action is sued for small or nominal damages, he may have little incentive to defend vigorously, particularly if future suits are not foreseeable. Allowing offensive collateral estoppel may also be unfair to a defendant if the judgment relied upon as a basis for the estoppel is itself inconsistent with one or more previous judgments in favor of the defendant. Still another situation where it might be unfair to apply offensive estoppel is where the second action affords the defendant procedural opportunities unavailable in the first action that could readily cause a different result.[7]

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7. "If, for example, the defendant in the first action was forced to defend in an inconvenient forum and therefore was unable to engage in full scale discovery or call witnesses, application of offensive collateral estoppel may be unwarranted. Indeed, differences in available procedures may sometimes justify not allowing a prior judgment to have estoppel effect in a subsequent action even between the same parties, or where defensive estoppel is asserted against a plaintiff who has litigated and lost." *Parklane*

(Cont'd)

> We have concluded that the preferable approach for dealing with these problems in the federal courts is not to preclude the use of offensive collateral estoppel, but to *grant trial courts broad discretion to determine when it should be applied.*

Parklane Hosiery Co., Inc., 439 U.S. at 326-31, 99 S.Ct. 645, 58 L.Ed.2d 552 (citations, footnotes, internal quotation marks omitted) (emphasis added). Significantly, the Supreme Court expressly held: "The general rule should be that in cases where a plaintiff could easily have joined in the earlier action or where, *either for the reasons discussed above or for other reasons*, the application of offensive estoppel would be unfair to a defendant, a trial judge should not allow the use of offensive collateral estoppel." *Id.* at 331, 99 S.Ct. 645 (emphasis added).

Accordingly, even when the traditional prerequisites for collateral estoppel are satisfied,[8] trial courts have

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Hosiery Co., Inc., 439 U.S. at 331, 99 S.Ct. 645 (citations omitted). As discussed below, rather than affording Horton with additional procedural opportunities, the FAA's narrow scope of review deprived Horton of the procedural opportunities available in district court to attack a collateral estoppel-based judgment should the underlying judgment be vacated or reversed on appeal.

8. The prerequisites for offensive non-mutual collateral estoppel are whether "(1) there was a full and fair opportunity to litigate the identical issue in the prior action; (2) the issue was actually litigated in the prior action; (3) the issue was decided in a

(Cont'd)

"broad discretion" to decide whether to apply offensive non-mutual collateral estoppel. *Id.* Indeed, where "the application of offensive collateral estoppel would be unfair to a defendant, a trial judge *should not* allow the use of collateral estoppel." *Id.* (emphasis added); *see also Eureka Fed. Sav. & Loan Ass'n v. Am. Cas. Co.*, 873 F.2d 229, 234 (9th Cir.1989) ("[I]t is inappropriate to apply collateral estoppel when its effect would be unfair.").

We discern no basis for denying arbitrators the same broad discretion possessed by district courts. Accordingly, we hold (1) "[a]rbitrators are not free to ignore the preclusive effect of prior judgments under the doctrines of res judicata and collateral estoppel,"*Aircraft Braking Sys. Corp.*, 97 F.3d at 159, (2) arbitrators are entitled to determine in the first instance whether the prerequisites for collateral estoppel are satisfied, *id.*, and (3) arbitrators possess broad discretion to determine when they should apply offensive non-mutual collateral estoppel. *See Parklane Hosiery Co., Inc.*, 439 U.S. at 331, 99 S.Ct. 645.

IV.

We have held that a final judgment retains its collateral estoppel effect, if any, while pending appeal. *See Tripati v. Henman*, 857 F.2d 1366, 1367 (9th Cir.1988)

(Cont'd)

final judgment; and (4) the party against whom [collateral estoppel] is asserted was a party or in privity with a party in the prior action." *Syverson v. IBM*, 472 F.3d 1072, 1078 (9th Cir.2007) (citations omitted).

(stating that a pending appeal does not affect a judgment's finality for preclusion purposes). This rule creates the potential for a collateral estoppel-based judgment based on a prior judgment that is subsequently vacated or reversed on appeal. *See* Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, 18A Federal Practice & Procedure: Jurisdiction 2d. § 4433 (2002). Indeed, "in some cases, litigants and the courts have collaborated so ineptly that the second judgment has become conclusive even though it rested solely on a[prior] judgment that was later reversed." *Id.* (citing *Reed v. Allen*, 286 U.S. 191, 196-201, 52 S.Ct. 532, 76 L.Ed. 1054 (1932)). In the context of district court litigation, this potential problem can be "avoided, whether by delaying further proceedings in the second action pending conclusion of the appeal in the first action, by a protective appeal in the second action that is held open pending determination of the appeal in the first action, or by a direct action to vacate the second judgment." *Collins*, 361 F.Supp.2d at 1096 (citing Wright & Miller § 4433). Accordingly, we have held that the benefits of giving a judgment preclusive effect pending appeal outweigh any risks of a later reversal of that judgment. *See Tripati*, 857 F.2d at 367.

Here, the arbitrators were faced with a different, albeit similar, question. Specifically, they were faced with the question whether a judgment pending appeal should be given preclusive effect in an arbitration, a question that appears to be one of first impression in all jurisdictions.

The arbitrators recognized the district court's judgment as final,[9] but proceeded not to apply offensive non-mutual collateral estoppel because the FAA's narrow scope of review limits the ability of an arbitration defendant to overturn a collateral estoppel-based arbitration award in the event the judgment upon which it is based is vacated or reversed on appeal. *See Collins*, 361 F.Supp.2d at 1089-90. Our case law supports the drawing of such a distinction:

> Indeed, there are fundamental differences between confirmed arbitration awards and judgments arising from a judicial proceeding. Absent an objection on one of the narrow grounds set forth in sections 10 or 11,[10] the

9. The arbitrators' concern that the Hickcox judgment was on appeal was not inconsistent with an understanding that the Hickcox judgment was final for collateral estoppel purposes. Indeed, the arbitrators would not have relied on the equities underlying the case to reach their decision had they simply denied Appellants' motion for summary judgment based on any one of the *Syverson* factors.

10. "Sections 10 and 11 [of the FAA] permit a district court to vacate or modify an arbitration award under limited circumstances *unrelated to the merits*. For example, a court may vacate an award procured by corruption, fraud or undue means or rendered by a partial or corrupt arbitrator. *See* 9 U.S.C. § 10(a)(1), (2). Also, a court may modify an award to correct an obvious material miscalculation of figures

(Cont'd)

> [FAA] requires the court to enter judgment upon a confirmed arbitration award, without reviewing either the merits of the award or the legal basis upon which it was reached. A judgment upon a decision or order rendered by the court at the conclusion of a judicial proceeding, by contrast, confirms the merits of that decision. Along the same lines, a judgment under § 13 of the FAA is not subject to Federal Rules of Civil Procedure 59 or 60 whereas a judgment arising from a judicial proceeding is subject to reopening and challenge under those rules. And, unless the provisions of the parties' agreement provides to the contrary, there is no right under the FAA to appeal the merits of a confirmed arbitration award. In sum, a judgment upon a confirmed arbitration award is qualitatively different from a judgment in a court proceeding, even though the judgment is recognized under the FAA for enforcement purposes.

(Cont'd)

> or an imperfection in matter of form *not affecting the merits. See* 9 U.S.C. § 11(a), (c)." *Chiron Corp. v. Ortho Diagnostic Sys., Inc.*, 207 F.3d 1126, 1134 n. 2 (9th Cir.2000) (emphases added).

Chiron Corp., 207 F.3d at 1133-34.

We need not, however, resolve the question whether the arbitrators abused their discretion when they determined the qualitative difference between a district court judgment and an arbitration award rendered the application of offensive non-mutual collateral estoppel unfair. Rather, we resolve this case on the basis that "[t]he governing law alleged to have been ignored by the arbitrators [was not] *well defined, explicit, and clearly applicable.*" *See Carter*, 374 F.3d at 838 (emphasis added). In short, the arbitrators could not manifestly disregard the law because no binding precedent existed as to whether (1) arbitrators are required to afford federal judgments preclusive effect, (2) arbitrators possess the same broad discretion as district courts in determining whether to apply offensive non-mutual collateral estoppel, and (3) the qualitative difference between a district court judgment and an arbitration award renders unfair the application of offensive non-mutual collateral estoppel in arbitration on the basis of a prior judgment pending appeal.

AFFIRMED.

APPENDIX B — OPINION OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF ARIZONA DATED MARCH 21, 2005

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

No. CV-99-0330-PHX-ROS

JULIE E. COLLINS, *et al.*,

Plaintiffs,

v.

D.R. HORTON, INC.,

Defendant.

March 21, 2005

ORDER

SILVER, District Judge.

Plaintiffs Julie E. Collins ("Collins") and Robert B. Ryan ("Ryan") move this Court pursuant to 9 U.S.C. §§ 9 and 10 for an order confirming in part and vacating in part an arbitration award issued on October 10, 2003. For the reasons stated below, the Motion to Confirm in Part is partially granted and partially denied. The Motion to Vacate in Part is denied.

Appendix B

BACKGROUND

Defendant D.R. Horton, Inc. ("Horton") is a homebuilding company with operations in several states. (Compl. ¶ 10 [Doc. # 1]). In 1997, the company signed a merger agreement with Continental Homes Holding Corporation ("Continental"), a company in the homebuilding and home mortgage business located in Scottsdale, Arizona. (*Id.* ¶¶ 7, 13.)

In anticipation of the merger, Continental decided to enter into employment agreements with certain of its employees. (*Id.* ¶ 18.)The agreements were designed to induce the employees to stay on with the merged company for at least a period of time sufficient to accomplish the merger and the related combination of operations. (*Id.*)

Among those who entered into employment agreements were Plaintiffs Collins and Ryan and nonparty W. Thomas Hickcox ("Hickcox"). (*Id.* ¶ 17, 38; Exh. A to Pl.'s Mot. [Doc. # 229].) Collins was Continental's Chief Financial Officer, Treasurer, and Secretary. (Compl.¶ 9.) Ryan was the Vice President of Management Information Systems and a member of the Board of Directors. (*Id.*) Hickcox was Continental's Chief Executive Officer. (Exh. A to Pl.'s Mot.)

Among other things, Plaintiffs' employment agreements set forth the severance payments Plaintiffs would receive in the event their employment was terminated with or without cause (Compl.¶¶ 19, 41.) The

agreements also set forth the payments Plaintiffs would receive if they resigned during the term of the agreements for "good reason." (*Id.*) Hickcox's agreement contained similar provisions. (07/02/01 Order at 4 [Doc. # 170].)

As negotiations over the merger continued, an issue arose concerning whether Continental employees would be able to accelerate vesting of their stock options at the time of the merger. (Compl.¶ 66.) The proposed form of the merger did not allow for acceleration. (*Id.*) Plaintiffs allege that—to induce support for the merger—Horton verbally promised them and other Continental employees that it would give them 30,000 shares of its stock to offset the loss of their unvested options. (*Id.*)

The Continental-Horton merger became effective in April 1998. (*Id.* ¶ 13.) In November 1998, Horton notified Hickcox that it was terminating him without cause. (*See* 07/02/01 Order at 2.) Shortly thereafter, Collins and Ryan resigned their positions in the company, invoking the "for good reason" provision in their employment agreements. (Compl.¶¶ 34, 56.)

On February 22, 1999, Hickcox filed suit against Horton in this District, alleging breach of contract, failure to pay wages, promissory estoppel, and fraud. (*Hickcox v. D.R. Horton, Inc.*, CV-99-239-PHX-SRB.) The lawsuit was assigned to Judge Earl H. Carroll and later transferred to Judge Susan R. Bolton. Hickcox claimed that Horton miscalculated the severance

payments due under the provision of his employment agreement governing terminations without cause. (07/02/01 Order at 2.) He also claimed that Horton had refused to provide him with his portion of the 30,000 shares of stock it allegedly promised. (*Id.*)

That same day, Collins and Ryan jointly filed suit against D.R. Horton in this District, also alleging breach of contract, failure to pay wages, promissory estoppel, and fraud. This Court received the assignment. Collins and Horton claimed that they had resigned for "good reason" and that Horton had refused to pay them severance pay and benefits due under their employment agreements. (Compl.¶¶ 36, 58.) Like Hickcox, Collins and Ryan further claimed that Horton had reneged on its alleged 30,000-share promise. (*Id.* ¶¶ 66-70.)

On May 14, 1999, Horton moved in *Hickcox* to dismiss the plaintiff's claims and compel arbitration based on the compulsory arbitration provision in the parties' employment agreement. On May 27, 1999, however, the Ninth Circuit held that the Federal Arbitration Act ("FAA") does not apply to employment contracts and that compulsory arbitration provisions in such contracts were unenforceable. *See Craft v. Campbell Soup Co.*, 177 F.3d 1083, 1093 (9th Cir.1998). The *Hickcox* court thus denied the motion to dismiss. Horton did not move to compel arbitration in *Collins*, but preserved the contractual agreement to arbitrate as an affirmative defense.

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The *Hickcox* and *Collins* actions thereafter proceeded through discovery and to the dispositive motion phase. Collins and Ryan moved for partial summary judgment in *Collins* on July 31, 2000, and Horton cross-moved for partial summary judgment on August 2, 2000. On December 12, 2000, Hickcox and Horton each filed motions for partial summary judgment in *Hickcox*.

On December 27, 2000, Horton moved to consolidate the *Hickcox* and *Collins* actions, arguing, among other things, that both cases involved an alleged breach of a verbal promise to provide the plaintiffs with 30,000 shares of Horton stock. (Exh. A. to Pl.'s Mot. at 6.) Judge Bolton acknowledged that the contract and fraud claims arising out of the alleged promise presented a common issue, but denied the motion to consolidate based on differences in the parties wage claims. (07/02/01 Order at 5.)

In a decision entered on March 30, 2001 and in a written opinion entered on August 31, 2001, this Court denied the cross-motions for partial summary judgment filed in *Collins*. On July 23, 2001, Judge Bolton granted summary judgment in favor of Horton on some of the plaintiff's claims in *Hickcox*, but found the remaining claims survived summary judgment and required a trial. This Court scheduled a bench trial in *Collins* to begin on May 14, 2002. Judge Bolton scheduled a jury trial in *Hickcox* to begin on March 12, 2002.

In the meantime, on March 31, 2001, the United States Supreme Court issued its decision in *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 121 S.Ct. 1302, 149 L.Ed.2d 234 (2001), a case that had been appealed from the Ninth Circuit. The Supreme Court held that, contrary to the Ninth Circuit's reasoning in *Craft*, the FAA does apply to employment contracts (except contracts for employment of transportation workers) and that otherwise valid compulsory arbitration provisions were enforceable. On July 30, 2001, Horton moved to dismiss the *Collins* action and compel arbitration based on the ruling in *Circuit City*.The Court granted the Motion on March 29, 2002.

On March 28, 2002, the day before the Court entered its Order compelling arbitration, a jury returned a verdict in favor of the plaintiff in *Hickcox* on the contract and fraud claims related to Horton's alleged promise to transfer 30,000 shares. (*See* 03/05/03 Order at 2-3 [Doc. # 223].) The jury awarded Hickcox $87,500.00 in compensatory damages (representing the value of Hickcox's portion of the 30,000 shares as stipulated by the parties at trial) and $4,100,000.00 in punitive damages. (*Id.* at 3.) Judge Bolton later remitted the punitive damage award to $1,000,000.00 but rejected other efforts to overturn the verdict. (*Id.*)

On May 21, 2002, Collins and Ryan moved this Court to reconsider its Order compelling arbitration with respect to its claims arising out of the alleged 30,000-share promise. (03/05/03 Order at 3.) They argued that those claims were not arbitrable. (*Id.* at 4-7.) They

further argued that collateral estoppel barred relitigation of issues relating to those claims and that the issue of collateral estoppel should be decided by a judge rather than an arbitrator. (*Id.* at 7-14.) The Court denied the motion on March 5, 2003, finding that both the claims and the question of collateral estoppel should be submitted to the arbitrators. (*Id.* at 15.)

Collins and Ryan arbitrated their claims before a panel of three arbitrators in May 2003. Before the evidentiary hearing, they asked the arbitrators to apply collateral estoppel to their contract and fraud claims involving Horton's alleged promise of 30,000 shares, based on the *Hickcox* judgment. (*See* Exh. F. to Pls.' Mot.) In an order dated April 9, 2003, the arbitrators refused to treat the *Hickcox* judgment as final because the judgment was on appeal. The relevant text of the order reads as follows:

> "The arbitrators have considered all of the pleadings and documents that the parties have agreed might be considered in addressing the argument of Plaintiffs Collins and Ryan that collateral estoppel (issue preclusion) should be attributed in this arbitration to the resolution of various issues against Defendant D.R. Horton in the Hickcox case."
>
> "Although the argument for collateral estoppel to at least some issues might be compelling if this were an appealable proceeding in a court of law, the arbitrators conclude that collateral

estoppel should *not* be applied in this binding arbitration. The reason is that an appeal is pending in the Hickcox matter, an appeal that we gather will not be resolved until well beyond the projected end of the current proceeding. We recognize that the pendency of—and possible reversal in—an appeal would not necessarily deprive a judgment of preclusive effect in a collateral proceeding in a court of law. There, the availability of an appeal of the second proceeding would permit the estoppel to be undone and the second judgment to be set aside if the prior judgment were ultimately reversed. Practicality and fairness suggest a different conclusion in this binding arbitration, however, in which the estoppel, if now ordered, cannot later be undone if the Hickcox judgment is later reversed. Such, in any event, is our understanding, and on the basis of that understanding, we rule as follows:

> Subject to reconsideration if the Hickcox appeal is resolved before the conclusion of these proceedings, IT IS ORDERED denying the motion of Plaintiffs Collins and Ryan that collateral estoppel be attributed in this matter to issues resolved against Defendant D.R. Horton in the Hickcox case."

(Exh. G. to Pl.'s Mot.)

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On October 5, 2003, the arbitration panel issue its Final Award. (Exh. H. to Pls.' Mot.) The panel found for Collins and Ryan on the breach-of-contract claims related to wages and awarded $806,344.00 to Collins and $917,574.00 to Ryan, plus attorneys' fees, costs, and interest. (*Id.*) On the contract and fraud claims arising out of the alleged 30,000-share promise, however, the arbitrators reviewed the evidence and found against Collins and Ryan—a result that appears inconsistent with the verdict and judgment in the *Hickcox* action. (*Id.*)

On October 29, 2003, Collins and Ryan filed the instant Motion, seeking to confirm the portion of the arbitration award that was in their favor (the award on the wage claims) and to vacate the portion of the award that was not in their favor (the denial of the contract and fraud claims related to the 30,000 shares). With respect to the award on the wage claims, Collins and Ryan ask the Court to confirm that interest accrues on their gross (and not after-tax) wages. With respect to the alleged 30,000-share promise, Collins and Ryan argue that the arbitrators acted in manifest disregard of the law by failing to apply collateral estoppel. They ask that the Court enter judgment in their favor on those claims and award compensatory and punitive damages.

Horton filed its Response on December 2, 2003. As a preliminary matter, it argues that the Court lacks jurisdiction over the Plaintiffs' Motion because: (1) final judgment was deemed entered in this case no later than August 5, 2003, and (2) Plaintiffs' Motion does not comply with the notice and service provisions of 9 U.S.C. § 9. As

for the issue concerning interest, Horton argues that the matter should be resubmitted to the arbitrators. Concerning the 30,000-share promise, Horton points to the narrow standard of review (manifest disregard) and asserts that the arbitrators decision fell within that standard.

In their Reply in support of their Motion, Collins and Ryan for the first time argued that Horton had waived the argument that interest should be paid on net rather than gross wages.[1] They also for the first time argued that the Court should award them interest at the statutory rate of 10% on any unpaid liquidated amounts pursuant to Ariz.Rev.Stat. § 44-1201. The Court, in its discretion, decided to hear these arguments and on September 29, 2004 ordered the parties to provide supplemental briefing. The briefing is now complete, and the Court now turns to the Motion.

DISCUSSION

I. Jurisdiction

At the outset, the Court rejects Horton's challenge to this Court's jurisdiction to review and enter judgment

1. As Collins and Ryan later pointed out, their waiver argument was discussed in Exhibit K to their Motion, though not in the body of their memorandum of facts and law as required by Local Civil Rule 7.2. This is not sufficient to put the Court on notice of the argument. *See Greenwood v. FAA*, 28 F.3d 971, 977 (9th Cir.1994) (court reviews only issues specifically and distinctly argued in a party's brief)

on the arbitrator's award. Horton's first argument—that this case number is "long over"—turns on a mistaken view of finality. While it is true that the Court dismissed Plaintiffs' claims in favor of arbitration on March 3, 2004, and that judgment was deemed entered pursuant to Fed.R.Civ.P. 58(b) no later than August 4, 2003, courts have held that once a court obtains jurisdiction in an action and enters an order compelling arbitration, that court retains jurisdiction with respect to subsequent motions to confirm or vacate. *See Smiga v. Dean Witter Reynolds, Inc.*, 766 F.2d 698, 705 (2d Cir.1985); *T & R Enter. v. Continental Grain Co.*, 613 F.2d 1272, 1279 (5th Cir.1980); *Allen Group, Inc. v. Allen Deutschland GMBH*, 877 F.Supp. 395, 399 (W.D.Mich.1994); *Tesoro Petroleum Corp. v. Asamera*, 798 F.Supp. 400, 403 (W.D.Tex.1992). Although there is no Ninth Circuit case on point, the Court has not found any authority to the contrary. Plaintiffs' Motion satisfies jurisdictional requirements.

Horton's next argument—that Plaintiffs' Motion is procedurally defective because it was not filed and served precisely in the manner set forth in section 9 of the Federal Arbitration Act ("FAA"), 9 U.S.C. § 9—is similarly unpersuasive. 9 U.S.C. § 9 requires parties seeking confirmation of an arbitration award to file an "application" for confirmation in the district court within which the award was made and to serve notice of the application upon the adverse party. If the adverse party is a nonresident, then "notice of the application shall be served by the marshal of any district within which the adverse party may be found in like manner as other

process of the court." 9 U.S.C. § 9. Once notice of the application is served, "the court shall have jurisdiction of such party as though he had appeared generally in the proceeding." *Id.*

Horton's complaint that Plaintiffs' filed a "motion" rather than an "application" elevates form over substance. Although Plaintiffs' Motion was not labeled an "application," the Ninth Circuit has held in related situations that " 'nomenclature is not controlling.' " *W. Employers Ins. Co. v. Jeffries & Co.*, 958 F.2d 258, 260-61 (9th Cir.1992) (quoting *Sea Ranch Ass'n v. Cal. Coastal Zone Conservation Comm'ns*, 537 F.2d 1058, 1061 (9th Cir.1976)). The Motion meets the requirements of Rule 7(b)(1) of the Federal Rules of Civil Procedure—it states with particularity the grounds for the motion and the relief sought. There is no question that Horton was on notice of Plaintiffs' intent. It filed an opposition to Plaintiffs motion and clearly comprehends the relief requested. Further, Rule 7(b)(1) specifically states an "application to the court for an order shall be by motion." Under these circumstances, the fact that Plaintiffs' did not call their papers an "application" is immaterial.

The fact that Plaintiffs served their papers by mail rather than by a U.S. Marshal is also of no consequence. The parties agreed to waive formal service by stipulating in §§ 13 and 16 of their employment agreements to notice by mail and to the American Arbitration Associations Rules and Regulations, which state, "for any court actions in connection" with the arbitration, "each party shall be deemed to have consented" to service by mail.

(*See* Exhs. 1 and 2 to Pls.' Mot.) Plaintiffs provided sufficient and legally appropriate notice to Horton by mailing a copy of their Motion to Horton's counsel.

I. The Motion to Confirm and Vacate

A. Standard of Review

Courts play a limited role in reviewing arbitrator's decisions. Larry E. Edmonson, *Domke on Commercial Arbitration* § 38:1 (3d ed.2003). "Since the goal of arbitration is to provide the parties an alternative to a lengthy and costly litigation process, a court reviewing an arbitration award is more deferential to the arbitrator's decision than an appellate court would be in reviewing a decision of a trial court." *Id.* "This deference is designed to prevent the arbitration process from being 'transformed from a commercially useful alternative method of dispute resolution into a burdensome additional step on the march through the court system.' " *Id.* (quoting *Flexible Mfg. Sys. Pty Ltd. v. Super Prods. Corp.*, 86 F.3d 96, 100 (7th Cir.1996)).

Section 9 of the FAA provides that a district court "must grant [an order confirming the decision of the arbitrator] unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title." 9 U.S.C. § 9. Section 10 of the FAA, 9 U.S.C. § 10, sets out four very narrow grounds upon which courts may vacate commercial arbitration awards. Those grounds are: "(1) where the award was procured by corruption, fraud or undue means; (2) where there was evident

partiality or corruption on the part of the arbitrators; (3) where the arbitrators were guilty of misbehavior by which the rights of any party have been prejudiced; or (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." 9 U.S.C. § 10.

On its face, § 10 of the FAA does not sanction judicial inquiry into the merits of commercial arbitration awards. Over time, however, courts have articulated a variety of non-enumerated grounds that, in rare circumstances, justify the nullification of a procedurally proper arbitral award. The most widely recognized non-enumerated ground is the "manifest disregard of the law" standard. That standard—the sole ground for vacatur raised in the Plaintiffs' Motion—was first articulated in *dicta* in the United States Supreme Court's opinion in *Wilko v. Swan*, 346 U.S. 427, 436-37, 74 S.Ct. 182, 98 L.Ed. 168 (1953), *overruled on other groundsRodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 109 S.Ct. 1917, 104 L.Ed.2d 526 (1989). There, the Court remarked that "the interpretations of the law by the arbitrators *in contrast to manifest disregard*, are not subject, in the federal courts, to judicial review for error in interpretation." *Id.* (emphasis added). Although the Supreme Court has not since given guidance on the contours of the standards, the federal circuit courts have incorporated the rule into arbitration jurisprudence.

The manifest disregard standard is "both limited and highly deferential." *Sheet Metal Workers' Int'l Ass'n v.*

Madison Indus., Inc., 84 F.3d 1186, 1190 (9th Cir.1996). Satisfaction of the standard requires "something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand and apply the law." *San Martine Compania De Navegacion, S.A. v. Saguenay Terminals Ltd.*, 293 F.2d 796, 801 (9th Cir.1961). A court may not reverse an arbitration award even in the face of an erroneous interpretation of the law. *A.G. Edwards v. McCollough*, 967 F.2d 1401, 1403 (9th Cir.1992). Rather, to demonstrate manifest disregard, the moving party must show that the arbitrator "underst [oo]d and correctly state[d] the law, but proceed[ed] to disregard the same." *San Martine Compania De Navegacion*, 293 F.2d at 801.

B. Analysis

1. Confirmation of the Award on the Wage Claims

Before turning to whether the arbitrators' refusal to address the merits of the Plaintiffs' collateral estoppel argument constituted manifest disregard, the Court turns first to the question of whether it should confirm that portion of the arbitration award related to Plaintiffs' wage claims and request for fees and costs. The arbitration panel found in favor of Collins and Ryan on the wage claims and awarded $806,344.00 to Collins and $917,574.00 to Ryan, plus attorneys' fees, costs, and interest. Plaintiffs request that the Court enter partial final judgment on this portion of the award under 9 U.S.C. § 9 and Rule 54(b) of the Federal Rules of Civil Procedure. Three issues require the Court's resolution:

(1) whether Plaintiffs' request for partial confirmation has been rendered moot by Horton's payment of the amounts not in dispute, (2) whether interest must be paid on the gross (pre-tax) or net (post-tax) amount of the award, and (3) whether Plaintiffs' are entitled to pre-confirmation, post-award interest on any unpaid amounts.

Horton argues that Plaintiffs' request for confirmation is spurious because Plaintiffs have already been paid the arbitration award, with the exception of the amounts at issue in the parties dispute over interest. This argument is unavailing. Regardless of whether the undisputed amounts have already been paid, Plaintiffs are still entitled to an order confirming those amounts. 9 U.S.C. § 9 is phrased in mandatory terms. It provides that, upon application, a district court "*must* grant [a confirmation] order" unless the arbitration award is modified, vacated, or corrected. 9 U.S.C. § 9 (emphasis added). The mere fact that Horton has satisfied a portion of its obligation under the arbitration award does not divest the court of authority to confirm that portion of the award-satisfaction and confirmation are separate issues. *See District Council No. 9 v. APC Painting, Inc.*, 272 F.Supp.2d 229, 239 (S.D.N.Y.2003) (holding that the fact that the defendant had satisfied the arbitration awards at issue was irrelevant to whether the court should confirm the awards under 9 U.S.C. § 9.)

As for the parties' dispute concerning whether Horton must pay interest on the gross or net amount of the award, Horton has waived the argument that interest

should be paid only on net wages. The record shows that the arbitration panel issued an Interim Award on July 31, 2003, awarding $806,344.00 to Collins and $917,574.00 to Ryan. (Exh. 1 to Pls.' Surreply in Supp. of Their Mot.) After the arbitration panel issued its Interim Award but before it issued the Final Award, Plaintiffs asked the panel to award interest on all amounts due them. (Exh. 5 to Pls.' Reply in Supp. of Their Mot. at 5 & Exh. C thereto.) In their application to the arbitrators, Plaintiffs used the gross amount of the award as the basis for their interest calculations. (*Id.*) In response, Horton submitted its own interest calculations—also based on the gross wage award—and disputed only the interest *rate* calculation. (Exh. 6 to Pls.' Reply in Supp. of Their Mot. at 29 & Exh. D thereto.) With the parties apparently in agreement on the amount to which interest would be applied, the panel issued a Final Award that specifically addressed the interest *rate*. Consistent with parties' previous submissions, the Final Award granted the Plaintiffs prejudgment interest on the *entire* principal sum awarded to them, stating: "Horton shall pay to Plaintiff Collins the principal sum of . . . $806,344.00 [and $917,574.00 to Ryan], plus interest [on] each component of this sum." (Exh. H to Pls.' Mot. at 2-3, 5.)

Horton now seeks to retreat from its tacit acceptance in arbitration of the gross wage award as the basis for the interest calculations. It may not do so now. Federal courts have taken a dim view of parties raising arguments before the district court that were not made before the arbitrators. It is well settled that "[p]arties to arbitration proceedings cannot sit idle while an

arbitration decision is rendered and then, if the decision is adverse, seek to attack the award collaterally on grounds not raised before the arbitrator." *USWA v. Smoke Craft, Inc.*, 652 F.2d 1356, 1360 (9th Cir.1981). The utility of settling disputes by arbitration would be seriously undermined if the parties kept arguments from the arbitrators and then later attempted to undermine the award in federal court using those arguments. Horton never argued to the arbitrators, as it could have, that interest should be paid on net wages rather than gross wages. In fact, it specifically used gross wages when making its interest calculations. Horton's argument that interest should be paid only on net wages has been waived.

Having resolved that Plaintiffs are entitled to interest on the gross wage award, the Court next addresses Plaintiffs' request for post-award, pre-confirmation interest on the unpaid interest. Citing Ariz.Rev.Stat. § 44-1201, Plaintiffs argue that they are entitled to interest as a matter of right at the rate of ten percent per annum from the date of the award through the date of confirmation on the amount of interest disputed in this Motion. Horton argues that it owes no additional interest because the disputed amount was not liquidated, in light of the parties' disagreement over the amount of interest owed and the need for this Court's intervention. It further argues that, even if the amount was liquidated, its unconditional tender of the undisputed amount of the award stopped interest from accruing on the disputed portion.

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State law determines entitlement to, and the rate of, post-award, pre-confirmation interest in diversity actions enforcing arbitration awards under the FAA. *Northrop Corp. v. Triad Int'l Marketing S.A.*, 842 F.2d 1154, 1155 (9th Cir.1988). Under Arizona law, which the parties agree applies, " 'prejudgment interest on a liquidated claim is a matter of right.' " *AMHS Ins. Co. v. Mut. Ins. Co. of Ariz.*, 258 F.3d 1090, 1103 (9th Cir.2001) (quoting *Gemstar Ltd. v. Ernst & Young*, 185 Ariz. 493, 508, 917 P.2d 222, 237 (1996) (en banc)). Section 44-1201 of the Arizona Revised Statutes sets the interest rate at ten percent per annum. Where, however, a debtor in good faith contests the amounts due on a claim but makes an unconditional tender of the amount she contends is in fact owed, she stops interest from accruing on the disputed amounts. *Homes & Son Const. Co., Inc. v. Bolo Corp.*, 22 Ariz.App. 303, 306, 526 P.2d 1258, 1261 (Ariz.App.1974).

Plaintiffs are entitled to interest on the unpaid interest amount from October 5, 2003, the date of the Final Award, to October 24, 2003, when Horton wire transferred the undisputed amounts due. First, the Court rejects Horton's argument that the interest owed was not liquidated. An amount is liquidated when it becomes capable of exact calculation. *Ry-Tan Constr., Inc. v. Wash. Elem. Sch. Dist. No. 6*, 93 P.3d 1095, 208 Ariz. 379, 93 P.3d 1095, 1119-20 (Ariz.Ct.App.2004). The arbitrators granted pre-award interest on the entire principal sum awarded to Plaintiffs (the gross wage award). That interest was calculable as of the date of the Final Award and therefore liquidated, triggering

interest as a matter of right under Ariz.Rev.Stat. § 44-1201. Horton, however, stopped the clock on statutory interest October 23, 2003, when it paid all undisputed amounts owed-$1,015,808.72 to Collins and $1,133,677.82 to Ryan. *See Homes & Son Const. Co., Inc.*, 22 Ariz.App. at 306, 526 P.2d at 1261. There is no indication that Horton acted in bad faith in disputing the amount of interest owed. Plaintiffs thus are not entitled to statutory interest after October 23, 2003.

2. The Motion to Vacate

Plaintiffs' challenge to the arbitrators refusal to give the *Hickcox* judgment finality raises three main issues. First, if the parties had litigated their dispute in court rather than in an arbitral forum, would the refusal constitute reversible error? Second, were the arbitrators bound to give the *Hickcox* judgment preclusive effect or could they dispense with preclusion on fairness and practicality grounds? Third, assuming the arbitrators were required to treat the *Hickcox* judgment as final, did they manifestly disregard the law by failing to do so? The Court addresses each of these issues in turn.

a. Pending Appeals Do Not Deprive a Judgment of Preclusive Effect

There is no doubt that if the parties' dispute had been decided in court rather than in arbitration, the Court would have been required to treat the *Hickcox* judgment as final. The arbitrators did not accord the *Hickcox* judgment finality because of the pending appeal in that

matter. "The bare act of taking an appeal," however, "is no more effective to defeat preclusion than a failure to appeal." 18A Charles Alan Wright, Arthur R. Miller, & Edward H. Cooper, *Federal Practice & Procedure: Jurisdiction 2d.* § 4433 (2002). A final judgment retains all of its res judicata and collateral estoppel consequences pending decision of the appeal, apart from rare occasions when the appeal constitutes a proceeding *de novo. Id.; see also Tripati v. Henman*, 857 F.2d 1366, 1367 (9th Cir.1988) (stating that a pending appeal does not affect a judgment's finality for preclusion purposes). Thus, if this action had been decided this Court rather than arbitrated, the failure to accord the *Hickcox* judgment finality would have constituted reversible error.

Nevertheless, substantial difficulties arise from the rule that a trial court judgment retains its preclusive effects while an appeal is pending. "The major problem is that a second judgment based upon the preclusive effects of the first judgment should not stand if the first judgment is reversed." Wright, Miller & Cooper, *supra*, § 4433. "[I]n some cases, litigants and the courts have collaborated so ineptly that the second judgment has become conclusive even though it rested solely on a judgment that was later reversed." *Id.* (citing *Reed v. Allen*, 286 U.S. 191, 196-201, 52 S.Ct. 532, 76 L.Ed. 1054 (1932)). Wright, Miller, and Cooper counsel that "[t]his result should be avoided, whether by delaying further proceedings in the second action pending conclusion of the appeal in the first action, by a protective appeal in the second action that is held open pending

determination of the appeal in the first action, or by a direct action to vacate the second judgment." *Id.*

The arbitrators in this case recognized this problem; however, they chose to resolve it by dispensing with the *Hickcox* judgment and trying the claims related to the 30,000-share promise as if there had been no judgment (subject to reconsideration if the *Hickcox* appeal was resolved before the conclusion of the proceedings). Although Plaintiffs' argue that this decision was misguided, there are at the very least plausible arguments in support of it. None of the options suggested by Wright, Miller and Cooper work particularly well in the arbitration context. Staying resolution of the *Collins* arbitration pending an appeal in *Hickcox* would have undermined one of the main advantages of arbitration-avoidance of the delay of litigation. Delay is often "justice denied." Edmonson, *supra*, § 1.6. In contrast to the traditional adversarial method of dispute resolution, arbitration is intended to resolve disputes in a quick and cost-effective manner. *Id.*

Further, the parties would not have been able to vacate or reopen the arbitration award if the arbitrators had applied collateral estoppel on the basis of the *Hickcox* judgment and the *Hickcox* judgment was later reversed on appeal. When an arbitration award has been made, the authority of the arbitrators comes to an end. Edmonson, supra, § 37.2. A completed award generally cannot be modified, changed, or supplemented, except to clarify ambiguities in the award and mistakes apparent on the face of the award. *Id.* § 40.4. There is no

right to appeal the merits of an arbitration award absent the narrow grounds discussed in Section I(A) above, none of which would allow the award to be reopened on the basis of a reversal in *Hickcox*. And while Rules 59 or 60 of the Federal Rules of Civil Procedure might provide a procedural basis for a federal court to reopen a judgment that was based on collateral estoppel or res judicata if the judgment in the first action was reversed, these Rules do not apply to arbitrations. *See Chiron Corp. v. Ortho Diagnostic Sys., Inc.*, 207 F.3d 1126, 1133 (9th Cir.2000) (stating that a judgment under § 13 of the FAA is not subject to reopening and challenge under Rules 59 and 60). There are thus colorable arguments to support the position taken by the arbitrator's here.

At the same time, there are strong arguments in favor of applying collateral estoppel and res judicata in this situation as well. As Wright, Miller, & Cooper point out, "[d]espite the manifest risks of resting preclusion on a judgment that is being appealed, the alternative of retrying the common claims, defenses, or issues is even worse." Wright, Miller & Cooper, *supra*, § 4433. "All of the values served by res judicata [and collateral estoppel] are threatened or destroyed by the burdens of retrial, the potential for inconsistent results, and the occasionally bizarre problems of achieving repose and finality that may arise." *Id.* These difficulties are so great the federal courts have adopted the present rule: preclusion applies pending appeal, despite potential difficulties. Courts have found, quite simply, that benefits of giving a judgment preclusive effect pending appeal outweigh any risks of a later reversal of that judgment.

As Wright, Miller & Cooper put it: "Although there are disadvantages to relying on preclusion in such circumstances, the advantages are more important." Wright, Miller & Cooper, *supra*, § 4433 n. 24.

The disadvantages of denying a judgment preclusive effect pending appeal are apparent in this litigation. While the arbitrators likely intended to simplify the proceedings, they may have done just the opposite—require the parties to litigate issues that had long ago been decided. Further, they may also have produced an inconsistent result: the plaintiffs in *Hickcox* recovered on the 30,000-share promise while the Plaintiffs in this action—to whom the same promise was made at the same time—did not.[2]

b. Could the Arbitrators Refuse to Treat the *Hickcox* Judgment as Final?

Because the arbitrators had at least plausible arguments in favor of their position, the question then becomes: were they free to refuse to treat the *Hickcox*

2. The Court expresses no opinion on whether collateral estoppel in fact bars relitigation of issues related to the alleged 30,000 share promise, though as the arbitrators acknowledged in *dicta*,"the argument for collateral estoppel to at least some issues might be compelling . . ." (Exh. G. to Pl.'s Mot.) The issue before the Court at this stage is not whether Plaintiffs established all of the elements of collateral estoppel (full and fair opportunity to litigate, actually litigated and necessary to judgment, final judgment, and party or privity), but rather whether the arbitrators manifestly disregarded the law by refusing to even consider Plaintiffs' collateral estoppel argument because the *Hickcox* judgment was on appeal.

judgment as final on the basis of fairness and practicality? Stated differently, does the fact that this was an arbitration make a difference in terms of applicability of collateral estoppel? The answer is no—under federal law the arbitrators were bound to give the *Hickcox* judgment preclusive effect.

The Ninth Circuit has not specifically addressed whether arbitrators are bound by prior federal court decisions under the doctrines of collateral estoppel and/or res judicata, but other federal courts that have considered the issue have uniformly held that they are so bound. *See, e.g., Aircraft Braking Sys. Corp. v. Local 856*, 97 F.3d 155, 159 (6th Cir.1996) (holding that "arbitrators are not free to ignore the preclusive effect of prior judgments, although they generally are entitled to determine in the first instance whether to give the prior judicial determination preclusive effect"); *Miller v. Runyon*, 77 F.3d 189, 193 (7th Cir.1996) (Posner, J.) (noting that while the decisions are few, all but one, a state court case from Minnesota, support the applicability of res judicata and/or collateral estoppel in arbitrations); *John Morrell & Co. v. Local Union 304A*, 913 F.2d 544 (holding that collateral estoppel bars an arbitrator from reconsidering issues decided in prior judicial proceedings). The reasons for requiring arbitrators to apply res judicata and collateral estoppel are the same as those underlying the doctrines themselves—finality, protection of judgments, prevention of duplicative litigation, and avoidance of inconsistent results.

In this case, the arbitrators refused to consider the *Hickcox* judgment as final because fairness and practicality, in their view, counseled otherwise. Putting aside the case law discussed above for a moment and for the sake of understanding the arbitrators' decision, the arbitrators reliance on their sense of justice and equity does in fact have underpinnings in the ethos and law of arbitration. Arbitration is intended to provide a quicker and less expensive alternative to litigation. "It is similar to litigation in that it involves an adjudicative process including the presentation of proofs and arguments and the making of a decision by a third party." Murray S. Levin, *The Role of Substantive Law in Business Arbitration and the Importance of Volition*, 35 Am. Bus. L.J. 105, 106 (1997). But it is different in other respects. "Notably, the disputants, through their agreement to arbitrate, have the opportunity to design specific features of the process." *Id.* In court proceedings, for instance, there is a permanent body of procedural law which determines rights and obligations within a traditional legal framework. In agreements to arbitrate, however, the disputants can and do set the procedural rules. *Id.*

"Additionally, the disputants can designate the decision-making principles that are to be applied by the arbitrators in reaching their decisions"—the FAA and other arbitration statutes are silent on the role that substantive law is to play in arbitral decision-making. *Id.* This feature "raises some uncertainty about the role of substantive law in arbitration." *Id.* In a court of law, the judge decides the case based on the applicable rules

of substantive law. Judges strive to apply the law correctly because a prejudicial error can result in an appeal, negating a judgment. "In arbitration, arbitrators may be, but usually are not, directed to establish their decision on principles of substantive law." *Id.* Surprisingly, the extent to which arbitrators should and do apply substantive law in deciding cases remains unclear. *Id.*

Many state courts interpreting their own states' arbitration statutes, for instance, have expressed support for a process that of arbitral decision-making that is not controlled by substantive law. The California Supreme Court has held that "arbitrators, unless specifically required to act in conformity with rules of law, may base their decision on broad principles of justice and equity, and in doing so may expressly or impliedly reject a claim that a party might successfully have asserted in a judicial action." *Sapp v. Barenfeld*, 34 Cal.2d 515, 212 P.2d 233, 239 (1949). Other state courts have held that the arbitrators "may do justice as [they] see[ ] it, applying [their] own sense of law and equity,"*Silverman v. Benmor Coats, Inc.*, 61 N.Y.2d 299, 473 N.Y.S.2d 774, 461 N.E.2d 1261, 1266 (1984), may apply their own "notion of justice without regard to the applicable law,"*David Co. v. Jim W. Miller Const., Inc.*, 428 N.W.2d 590, 594 (Minn.Ct.App.1988), and may "fashion the law to 'fit the facts before them,' "*Israel Discount Bank Ltd. v. Rosen*, 169 A.D.2d 650, 565 N.Y.S.2d 29, 30 (N.Y.App.Div.1991) (quoting *Channel Textile Co. v. Adams*, 161 A.D.2d 409, 555 N.Y.S.2d 338, 338 (N.Y.App.Div.1990)).

Similarly, the American Arbitration Association ("AAA") has articulated rules that suggest that arbitrators should be less constrained to follow the law than judges and should be free to base decisions on equitable and practical considerations and on personal wisdom and experience.[3] Rule 43 of the AAA's National Rules for the Resolution of Employment disputes, for instance, states that in making an award an arbitrator is free to "grant any remedy or relief the arbitrator deems just and equitable." Am. Arbitration Ass'n, Nat'l Rules for the Resolution of Employment Disputes, Rule 43 (2004). "While this rule and other similarly worded AAA rules are more explicitly focused on the remedial function, they emphasize the arbitrator's sense of justice and equity, and thereby at least acknowledge that arbitrators are not obligated to apply the law rigidly." Levin, *supra*, at 114.

Other AAA publications provide additional insight on the perceived relationship between arbitration, legal rights, and the authority of arbitrators. In *Business Arbitration-What You Need to Know* 31 (rev.3d ed.1987), Robert Coulson, the former president of the AAA, remarks:

> It is sometimes said that arbitrators are not bound by the law in reaching their decisions.

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3. The AAA rules applied in this arbitration. The parties' employment agreements provided that any disputes under the agreements "shall be settled . . . in accordance with the applicable rules and procedures of the American Arbitration Association." (*See* Exh. 1 to Pls.' Mot. at 17.)

> This is misleading. Commercial arbitrators are carefully briefed by each opposing lawyer as to the applicable law. At the same time, attorneys argue the equitable and practical considerations that should be weighed by the arbitrator. It is improper for an arbitrator to refuse to listen to any pertinent arguments raised by either counsel. The arbitrator should carefully consider the legal arguments, even though not required to make findings on legal issues.

As Levin, *supra* at 117, observes, "this cautious statement epitomizes the ambiguous character of the interplay between law and arbitration." On the one hand, "we are told, [that arbitrators] are briefed on the law by adversaries and should listen to and consider legal arguments." *Id.* at 117-18. "[A]t the same time, the arbitrators are required to weigh other 'equitable and practical considerations,' and they are not required to report specific findings." *Id.* at 118. "Functioning primarily in this AAA environment, arbitrators have grappled with a process that includes presentation of law, but allows for, or at least tolerates, an overriding personal sense of justice." *Id.*

Against this backdrop, it is not surprising that the arbitrators grounded their refusal to accord the *Hickcox* judgment finality in fairness and practicality. Federal courts interpreting the FAA, however, have imposed a duty on arbitrators to follow the substantive law. John F.X. Peloso, *A Discussion of Whether Arbitrators Have*

a Duty to Apply the Law, 949 PLI/Corp. 61, 63 (July-Aug.1996). The manifest disregard of the law standard—which is not a basis for overturning an arbitration award in those jurisdictions that affirmatively hold that arbitrators are not required to base their decisions on the substantive law—presumes that arbitrators are bound by the law. *Id.* Further, the United States Supreme Court has stated that it assumes arbitrators will follow the law when ascertaining the basis for recovery in arbitration. In holding that pre-dispute arbitration agreements are enforceable, the Supreme Court, in *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 230-32, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987), stated that "there is no reason to assume . . . that arbitrators will not follow the law; although judicial scrutiny of arbitration awards necessarily is limited, such review is sufficient to ensure that arbitrators comply with the requirements of the [law]." More importantly—and more relevant with respect to the specific facts of this case—all federal courts that have considered the question have held that arbitrators are bound to give preclusive effects to prior federal court judgments. *See, e.g., Miller*, 77 F.3d at 193. The arbitrators were therefore not free to refuse to give the *Hickcox* judgment preclusive effect on the basis of their overriding sense of fairness and practicality.

c. Did the Arbitrators Manifestly Disregard the Law?

At the end of the day, the question is not whether the federal arbitrators erred, but whether they acted in

manifest disregard of the law.[4] Manifest disregard of the law is more than mere error in the law. *San Martine Compania De Navegacion, S.A.*, 293 F.2d at 801. As discussed above, federal courts give wide deference to the decisions of arbitrators. A corollary of the strong federal policy favoring arbitration is that "arbitration awards are particularly insulated from judicial review." *Container Prods. Inc. v. United Steelworkers*, 873 F.2d 818, 819 (5th Cir.1989). Applying the deferential manifest disregard standard to the facts of this case, the Court finds that vacatur of the arbitration award is not warranted.

To demonstrate a manifest disregard of the law, Plaintiffs must show that the arbitrator understood and correctly stated the law, but then proceeded to ignore it. *San Martine Compania De Navegacion, S.A.*, 293 F.2d at 801. The "manifest disregard" of the law standard thus has two elements. "One element looks to the result

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4. The Court may not, as Horton suggests, remand this matter to the arbitrators with instructions to consider the collateral estoppel issue. "Arbitrators are not and never were intended to be amenable to the 'remand' of a case for 'retrial' in the same way as a trial judge . . . It is [a] fundamental common law principle that once an arbitrator has made and published a final award his authority is exhausted and he is *functus officio* and can do nothing more in regard to the subject matter of the arbitration." *McClatchy Newspapers v. Cent. Valley Typographical Union No. 46*, 686 F.2d 731, 733-34 (9th Cir.1982). Limited exceptions exist for clarification of an award, completion of an incomplete award, and correction of mistakes that appear on the face of the award. *Id.* at 734. None of these exceptions apply here.

reached in the arbitration and evaluates whether it is clearly consistent or inconsistent with the controlling law." Stephen L. Hayford, *Reining in the 'Manifest Disregard Standard': The Key to Restoring Order to the Law of Vacatur*, 1998 J. Disp. Resol. 117, 124 (1998). To satisfy this element, "a reviewing court must conclude that the arbitrator misapplied or failed to apply the relevant law touching upon the dispute before her in a manner that constitutes a blatant, gross error of law that is apparent on the face of the award." *Id.* "[T]his component of the manifest disregard inquiry looks to an 'actus reus'—like dimension—the commission of a very serious error of law . . . by the arbitrator." *Id.*

But an error of law, "no matter how obvious or outrageous a court may deem it to be, cannot alone justify vacatur." *Id.* "That conclusion requires evaluation of the second element of the 'manifest disregard' of the law standard—the arbitrator's knowledge, her awareness of the relevant law and the manner in which she behaved in light of that knowledge." *Id.* This inquiry "takes the form of a two-dimensional 'mens rea'—like, state of mind determination." *Id.* That is, "the arbitrator must have been aware of the correct law and further must have consciously or intentionally chosen not to apply it to the facts of the case in rendering the award." *Id.*"Absent evidence in the record before the reviewing court reliably demonstrating that the arbitrator actually misapplied the relevant law and did so with knowledge of the error of that action and/or the intention to nullify the law or an awareness that he was doing so, vacatur is not appropriate." *Id.*

Here, Plaintiffs have satisfied the "actus reus" dimension of the manifest disregard of the law standard. As shown in the sections above, the arbitrators failure to accord the *Hickcox* judgment finality and concomitant refusal to address the merits of Plaintiffs' collateral estoppel argument constituted an error of law. Plaintiffs have not, however, satisfied the "mens rea" portion of the manifest disregard of the law test. To satisfy this element, the arbitrators must have understood that they were acting in error. *See San Martine Compania De Navegacion, S.A.*, 293 F.2d at 801. Here, there is no indication that the arbitrators understood that they were misapplying the law or intended to nullify the law when they decided to dispense with Plaintiffs' collateral estoppel argument on the basis of equitable considerations.

In fact, the evidence shows just the opposite—that the arbitrators misunderstood the law:

> "We recognize that the pendency of—and possible reversal in—an appeal would *not necessarily* deprive a judgment of preclusive effect in a collateral proceeding in a court of law. There, the availability of an appeal of the second proceeding would permit the estoppel to be undone and the second judgment to be set aside if the prior judgment were ultimately reversed. *Practicality and fairness suggest a different conclusion in this binding arbitration*, however, in which the estoppel, if now ordered, cannot later be undone if the

> Hickcox judgment is later reversed. Such, in any event, is *our understanding*, and on the basis of that understanding, we rule as follows . . ."

(Final Award, Exh. G. to Pl.'s Mot. (emphasis added).) The phrase "not necessarily" in the first sentence quoted above shows that the arbitrators did not recognize that the rule that a pending appeal does not deprive a judgment of preclusive effect has no exceptions. The second and third sentences, which attempt to distinguish the applicability of the rule in the arbitration context, show that the arbitrators did not understand the rule applies equally to arbitrations and to proceedings in a court of law. Finally, there is nothing in this paragraph to suggest that the arbitrators understood that general principles of fairness and practicality are not sufficient grounds to dispense with collateral estoppel under federal law. Rather, the arbitrators' decision indicates that they assumed that their invocation of fairness and practicality was perfectly acceptable and legal.

Given the AAA environment which encourages the arbitrators to weigh equitable and practical considerations, it is understandable that the arbitrators refused to treat the *Hickcox* judgment as final based on their view of justice and equity. Although Plaintiffs now complain that fairness and practicality are not grounds to refuse to apply collateral estoppel, there is no evidence in the record that they educated the arbitrators on this point. *See GMS Group, LLC v. Benderson*, 326 F.3d 75, 81 (2d Cir.2003) ("[T]he panel of arbitrators is a blank slate unless educated in the law by the parties.")

Although the arbitrators committed an error of law, the Court cannot conclude that the arbitrators understood they were acting in error. It therefore cannot find that the arbitrators acted in "manifest disregard of the law."

Accordingly,

IT IS ORDERED that Plaintiffs Julie E. Collins and Robert B. Ryan's Motion to Confirm in Part [Doc. # 229-1] is **GRANTED IN PART** and **DENIED IN PART**. The Court hereby **CONFIRMS** the arbitration award in all respects. It **FURTHER CONFIRMS** that Plaintiffs Julie E. Collins and Robert B. Ryan are entitled to interest on the gross (not the net) amount of the wage award. The Court **FURTHER ORDERS** that Plaintiffs Julie E. Collins and Robert B. Ryan are entitled to interest at ten percent (10%) per annum on their respective unpaid interest from October 5, 2003 to October 24, 2003. The Court **DENIES** Plaintiffs' request for statutory interest past October 24, 2003.

IT IS FURTHER ORDERED that Plaintiff Julie E. Collins and Robert B. Ryan's Motion to Vacate in Part [Doc. # 229-1] is **DENIED**.

IT IS FURTHER ORDERED that Plaintiff Julie E. Collins and Robert B. Ryan's Motion to Enter Judgment as a Matter of Law on Certain Contract and Fraud Claims Based on Collateral Estoppel [Doc. # 229-2] is **DENIED**.

IT IS FURTHER ORDERED directing the Clerk of the Court to enter judgment promptly in accordance with this Order.

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No. 07-849

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In The
Supreme Court of the United States

JULIE E. COLLINS AND ROBERT B. RYAN,

Petitioners,

v.

D.R. HORTON, INC.,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF IN OPPOSITION

E. KING POOR
Counsel of Record
QUARLES & BRADY LLP
500 West Madison Street
Suite 3700
Chicago, Illinois 60661-2511
(312) 715-5000

LONNIE J. WILLIAMS, JR.
C. CHRISTINE BURNS
QUARLES & BRADY LLP
One Renaissance Square
Two North Central Avenue
Phoenix, Arizona 85004-2391
(602) 229-5200

Attorneys for Respondent

COCKLE LAW BRIEF PRINTING CO. (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED

The question that petitioners have presented to this Court—whether a court or arbitrator should decide the preclusive effect of an earlier court judgment—is not an issue the Ninth Circuit ever decided. The reason for this is that petitioners never presented the question there. As shown further in Section I of the Argument, the petition should be denied for this reason alone.

CORPORATE DISCLOSURE

Pursuant to Supreme Court Rule 29(6), D.R. Horton, Inc. states that FMR Corporation owns more than 10% of its stock.

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ARGUMENT

I. The Ninth Circuit Never Reached The Question Presented Here and For Good Reason: Petitioners Never Presented It to the Ninth Circuit.

A. The Question Presented Before This Court Must Have Been Raised in the Court Whose Decision Is Under Review.

A fundamental rule of practice is that this Court does not decide questions that were never raised or decided in the court whose decision is under review. *Adickes v. Kress & Co.*, 398 U.S. 144, 148 n.2 (1970) (issues neither raised nor addressed by the court of appeals will not ordinarily be considered); *Pennsylvania Department of Corrections v. Yeskey*, 524 U.S. 206, 212-13 (1998) (Court refuses to address issue raised by petitioners, when it was not addressed by the district court or the court of appeals); *United States v. United Foods, Inc.*, 533 U.S. 405, 417 (2001) (when the argument was neither raised nor passed upon in the court whose opinion is under review, this Court will not address it.) In particular, a question presented in a petition for certiorari, but not raised in the court of appeals, is not properly before this Court. *Delta Airlines, Inc. v. August*, 450 U.S. 346, 362 (1981). The only exception to this general principle is when the lower court directly raises and addresses an issue *sua sponte*. *Virginia BankShares, Inc. v. Sandberg*, 501 U.S. 1083, 1099 n.8 (1991). As shown below, the question presented to this Court—whether a court or an arbitrator determines the preclusive

effect of a prior judgment—was never presented to the Ninth Circuit, and the Ninth Circuit never raised the question on its own.

B. The Question Presented Before This Court Was Never Addressed in the Ninth Circuit.

1. Though Petitioners Raised the Issue Before the District Court in 2003, They Failed to Raise It Again for the 2005 District Court Decision That the Ninth Circuit Reviewed.

In February 1999, petitioners filed suit against respondent alleging that it was liable for severance pay and benefits under their employment agreements and for an alleged promise to grant petitioners 30,000 shares of stock. C.R. 1.[1] In December 2000, respondent moved to consolidate this lawsuit with another action brought against it by another former employee, which alleged similar, though not identical claims. *Hickcox v. D.R. Horton, Inc.* (*Hickcox* Case). C.R. 159. Petitioners opposed the motion to consolidate on the grounds that the cases involved different factual and legal issues; the court denied consolidation. C.R. 160, 170.

In March 2001, this Court issued its opinion in *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105

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[1] Citations to the record refer to the clerk's record (C.R.) as set forth in the United States District Court for the District of Arizona, Civil Docket, Case No. 99-CV-330.

(2001), allowing arbitration provisions in employment agreements to be enforced under the Federal Arbitration Act ("FAA") and overruled the existing Ninth Circuit law which held that the FAA did not apply to employment contracts. Following the *Circuit City* decision, respondent moved to dismiss the case and compel arbitration. C.R. 171. The district court granted respondent's motion and dismissed petitioners' action in favor of arbitration. C.R. 219. Shortly after the district court entered its order compelling arbitration, a jury returned a verdict in favor of the plaintiff in the *Hickcox* Case. Pet. at 5-6.

In May 2002, petitioners moved the district court to reconsider its order compelling arbitration based on the fact that a jury verdict had been entered against respondent in the *Hickcox* Case. C.R. 220. Specifically, petitioners argued, among other things, that any relitigation of the claims arising out of the alleged promise of stock were barred by collateral estoppel, and that the issue of collateral estoppel should be decided by a judge rather than an arbitrator. *Id.* This was the first and only time during the eight-year history of this case that petitioners ever raised the issue of whether arbitrators could decide collateral estoppel issues. In March 2003, the district court issued an opinion denying petitioners' motion. *Collins v. D.R. Horton, Inc.*, 252 F. Supp.2d 936 (D. Ariz. 2003). C.R. 228. After an extensive discussion of the case law, the court held that the question of collateral estoppel could be decided by arbitrators. *Id.* at 944-45.

Petitioners then submitted their claims to arbitration and asked the arbitrators to apply collateral estoppel to the claims arising out of the *Hickcox* Case judgment. E.R. 229, Ex. F.[2] The arbitrators refused to apply collateral estoppel because the *Hickcox* Case judgment was on appeal. The arbitrators issued an award finding in favor of petitioners on the breach of contract claims and against petitioners on the fraud claims related to respondent's alleged promise to issue stock. E.R. 229, Ex. H.

Petitioners moved the district court to confirm in part and vacate in part the arbitrators' decision and enter judgment as a matter of law based on collateral estoppel. C.R. 229. With respect to the alleged promise of stock, petitioners argued solely that the arbitrators acted in "manifest disregard of the law" by failing to apply collateral estoppel and they requested that the district court enter judgment in their favor on those claims and award compensatory and punitive damages. Pet. App. at 41a, 51a.[3] Yet petitioners did not mention, much less argue, the issue of whether the court or arbitrator should determine the preclusive effect of a prior judgment. *Id.*

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[2] Documents filed in the Arbitration Proceedings are not identified as part of the District Court's Record. Therefore, citations to "E.R." refer to Petitioners' Excerpts of Record filed with their Ninth Circuit Brief.

[3] Reported at *Collins v. D.R. Horton, Inc.*, 361 F. Supp.2d 1085 (D. Ariz. 2005).

The district court confirmed the arbitration award in all respects. *Id.* at 56a. With the exception of merely mentioning the fact that petitioners raised the issue in their 2003 motion for reconsideration, the district court did not discuss whether a court or an arbitrator should decide the issue of collateral estoppel. *Id.* at 26a. Rather, the court focused on petitioners' argument that the arbitrators improperly failed to apply collateral estoppel, and in doing so they "manifestly disregarded" the law. *Id.* at 55a.

2. The Petitioners Never Raised the Issue in the Ninth Circuit.

The simplest way to test whether an issue was raised in the court of appeals is to look at the "issue presented" section of the opening brief. In this case, petitioners failed to raise the question of whether an arbitrator can decide collateral estoppel in that section of their opening brief. Instead, they described the issue as follows:

> Julie Collins, Robert Ryan, and Tom Hickcox were part of a management team that received, as a group, the same fraudulent promise from DRH, and they filed lawsuits alleging identical contract and fraud claims. DRH litigated and lost the first action brought by Hickcox. Collins' and Ryan's claims were then tried to arbitrators, who refused to apply collateral estoppel because DRH had appealed Hickcox's judgment. The district court found that the arbitrators had

> committed legal error in allowing DRH to relitigate the issues but held that they did not show "manifest disregard of the law" because they did not subjectively understand their error. Did the court err by failing to vacate the arbitration award?

Resp. App. at 2-3.[4] Petitioners do not quote or refer to the issue they presented to the Ninth Circuit in their petition. Rather, they piece together citations to other portions of their briefs to argue that the issue of whether an arbitrator can decide collateral estoppel issues was raised elsewhere. Pet. at 11, n.4.

Yet examining these page citations readily shows that the issue presented to this Court was never raised in the Ninth Circuit. Petitioners cite to four pages in their opening brief (pages 12-13 and 29-30) and one page in their reply brief (page 29) as supposed proof that they raised the issue below. Pet. at 11, n.4. Such citations cannot, however, be read to stand for the proposition that the issue was raised before the Ninth Circuit.

In particular, at pages 12-13 of their opening brief, petitioners argue only that the pendency of an appeal in the *Hickcox* Case did not excuse the arbitrators from applying collateral estoppel (Resp. App.

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[4] The pages which petitioners cite to argue that they raised the issue in the Ninth Circuit (*see* Petition at 11, n.4) as well as the Issue Presented from the opening brief in the Ninth Circuit are included in the appendix to this brief (Resp. App.).

at 3-5) and at pages 29-30 they argue against the district court's interpretation of the "manifest disregard" standard for reviewing arbitration awards. Resp. App. at 6-9. Similarly, at page 23 of their reply brief petitioners merely conclude their argument that the district court erred under the manifest disregard standard. Resp. App. at 11. Yet there is no argument in any of the cited pages, or anywhere else, that raises the issue of whether a court or an arbitrator should decide collateral estoppel issues.

As further evidence that the issue was not presented to the Ninth Circuit, the relief that petitioners request here is inconsistent with what they requested in the Ninth Circuit. There, petitioners requested that the court reverse the district court judgment and enter a judgment of damages in favor of petitioners in the same amount as the *Hickcox* Case. Appellants' Opening Br. at 24, 30. In contrast, as shown in Section IV below, a reversal by this Court could not result in an award of damages, but rather only a remand to have the district court weigh the factors as to whether collateral estoppel should apply to the facts of this case.

Finally, petitioners make a vague reference to the issue being raised at oral argument, but do not provide specific quotes, let alone the context. Pet. at 11, n.4. That is because the issue was not addressed at oral argument. Merely citing generally to the Ninth Circuit's audio file for oral argument is not evidence of anything. And it certainly does not support the argument that petitioners raised the issue there.

3. The Ninth Circuit Did Not Address the Issue.

Not only did petitioners themselves fail to raise the issue below, the Ninth Circuit never raised it *sua sponte*. Petitioners cite to one phrase contained in the Ninth Circuit's opinion in an attempt to argue the Ninth Circuit addressed the issue. Pet. at 12, Pet. App. at 17a. Petitioners state that the Ninth Circuit held that "arbitrators are entitled to determine in the first instance whether the prerequisites for collateral estoppel are satisfied" and imply that the Court issued this holding after first considering the issue of whether the court or the arbitrator should determine if collateral estoppel applies. Pet. at 12. However, petitioners take this phrase completely out of context.

In discussing the issue of whether arbitrators are bound by federal court decisions, the Ninth Circuit did in fact conclude that, based on this Court's opinion in *Parklane Hosiery Company, Inc.*, 439 U.S. 322, 332 (1979), "arbitrators are not free to ignore the preclusive effect of prior judgments under the doctrines of *res judicata* and collateral estoppel, although they generally are entitled to determine in the first instance whether to give the prior judicial determination preclusive effect." Pet. App. at 11a. Yet the Ninth Circuit never addressed whether the court or arbitrator should conduct the collateral estoppel analysis; rather it concluded that when conducting the analysis, an arbitrator must give preclusive effect to prior federal judgments where the prerequisites for collateral estoppel are satisfied. *Id.* at 16a-17a.

In sum, whether an issue was raised below should not require a search of the briefs, oral argument audio files and the opinion to determine if the issue could, under some reading, somehow be discerned. Here, if petitioners had actually raised the issue below, it would have been set forth directly on the first page of their opening brief and it would have been apparent from the overall argument in the briefs and from the opinion itself. Further, one oblique, passing reference to the issue that petitioners take out of context is obviously insufficient for the issue to be considered as having been raised *sua sponte*. As such, the Ninth Circuit never considered, weighed or ruled on the issue of whether an arbitrator or a court has the authority to decide the issue of collateral estoppel. The petition should be denied for this reason alone.

II. There Is No Recent or Well-Defined Division of Authority Among the Circuits as to Whether a Court or an Arbitrator Must Decide the Issue of Collateral Estoppel.

A. Some Decisions Deal With *Res Judicata*, Some With Collateral Estoppel, Some With State Law and There Is Hardly a Clear Split of Authority.

As shown in the last section, the petition should be denied for the threshold reason that the question presented was never raised or decided in the Ninth Circuit. Yet even if the merits of the petition could be considered, petitioners have not presented any

convincing reason to grant it. First, petitioners claim a division of authority between the Second, Eleventh and the Ninth Circuits that hold arbitrators may decide preclusion issues, and the Third, Fifth, and Eighth Circuits that supposedly hold that only courts may do so. Pet. at 13-14. Petitioners also cite a number of state court decisions addressing the issue (Pet. at 15), yet these may be safely ignored since this Court does not reconcile divergent opinions among state courts. Moreover, a review of the federal cases cited by petitioners shows no real division among the circuits.

First, the law of the Third, Fifth, and Eighth Circuits is far from holding that an arbitrator can never decide the issue of collateral estoppel. As to the Third Circuit precedent petitioners cite, the first case, *Telephone Workers Union v. New Jersey Bell Tel. Co.*, 584 F.2d 31 (3d Cir. 1978), is a 30-year old case involving an action to enforce an arbitration award after-the-fact, as opposed to compel arbitration. There, the court mentioned without analysis that when a court is presented with a question of whether an earlier judgment barred relitigation, the court would decide that issue. *Id.* at 32. The second case, *John Hancock Mutual Life Ins. Co. v. Olick*, 151 F.3d 132, 137 (3d Cir. 1993), dealt with *res judicata* which involves preclusion of an entire claim as opposed to the more limited effect of collateral estoppel which bars only individual issues. As shown below, the authority cited by petitioners notes a difference

between the two when it comes to arbitrators deciding preclusion issues.

Moreover, beyond these 15 and 30-year old cases, more recent authority from the Third Circuit has dispelled any notion that it would not allow arbitrators to decide preclusion issues. Most recently, in *Sherrock Bros., Inc. v. DaimlerChrysler*, 2008 WL 63300 (3d Cir. Jan. 7, 2008), the court held that arbitrators had correctly applied *res judicata* and collateral estoppel to determine that an earlier federal court judgment barred further litigation. *Id.* at *3. And even before *Sherrock*, the court in *Steris Corp. v. Int'l Union*, 489 F. Supp.2d 501, 512 (W.D. Pa. 2007) readily found that Third Circuit law allowed arbitrators to rule on such issues: "We conclude that the law of this Circuit [the Third] makes the preclusive effect of a prior arbitration an issue for an arbitrator to decide." Plainly, the Third Circuit cannot be counted to show any supposed split in authority.

This leaves the Fifth and Eighth Circuits. As to the Fifth Circuit, petitioners cite only one 22-year old decision, *Miller Brewing v. Fort Worth Distrib. Co.*, 781 F.2d 494, 499 (5th Cir. 1986). But *Miller Brewing* does not deal with federal law. Rather, there the court considered the *res judicata* effect of a state court judgment and the Fifth Circuit applied Texas law as to that. *Id.* at 498-99. As such, *Miller Brewing* has little precedential value when considering a division among the circuits on federal law.

Of the two Eighth Circuit cases cited by petitioners, neither squarely holds that an arbitrator can never decide preclusion issues. In *In re Y&A Group Sec. Litigation*, 38 F.3d 380 (8th Cir. 1994), the court stated that courts had the "power to defend their judgments as *res judicata*," but this statement was made in the limited context of a consent decree with an express injunction barring relitigation. *Id.* at 382. At the same time, one member of the panel, Judge Arnold, pointed out in a concurring opinion that the decision turned on this express reservation to bar future litigation, and therefore, "I do not read this Court's opinion today to hold generally that courts may, by injunction, control the decision of arbitrators on questions of issue or claim preclusion." *Id.* at 384.

The other Eighth Circuit case, *John Morrell & Co. v. Local Union 304*, 913 F.2d 544 (8th Cir. 1990), actually supports the opposite view. There, the court stated, "[w]e recognize that the arbitrator had the authority to determine *in the first instance* whether to give the prior judicial determination preclusive effect," and then reviewed the arbitrator's decision *after* it had made that determination. *Id.* at 562 (emphasis added). Thus, the law of the Eighth Circuit cannot be said to bar arbitrators from deciding preclusion issues.

Petitioners also overlook the difference between an arbitrator deciding issues of *res judicata* which involves an entire claim, and collateral estoppel, which involves only individual issues. Indeed, the law review article that petitioners cite (Pet. at 16), Jarrod

Wong, *Court or Arbitration—Who Decides Whether Res Judicata Bars Subsequent Arbitration Under the Federal Arbitration Act?*, 46 Santa Clara L. Rev. 49, 58-59 (2005)—despite its title—does *not* maintain that there is a split of authority at all; it actually argues that any supposed division can be "reconciled." *Id.* at 51. In particular, the author draws a distinction between a court giving *res judicata* effect to its *own* order versus an arbitrator deciding the preclusive effect of another court's judgment and argues that courts generally approve of both approaches. *Id.* at 51-52. The article makes a further distinction between an arbitrator deciding collateral estoppel issues and concludes that a court's need to protect its own judgment is "more limited in the context of collateral estoppel because it affects only issues and not entire claims," and therefore, "arbitrators rather than courts should determine the collateral estoppel effects of a prior decision." *Id.* at 91. *See also, Miller v. Runyon*, 77 F.3d 189, 193-94 (7th Cir. 1996) (court states *in dicta* that when deciding whether an arbitrator may decide preclusion issues, "a distinction must be made between *res judicata* and collateral estoppel"). Petitioners make no attempt to address the distinction between *res judicata* and collateral estoppel and cannot point to any real disagreement among the circuits as to whether arbitrators can decide collateral estoppel issues. *See, e.g., United States Fire Ins. Co. v. Nat'l Gypsum Co.*, 101 F.3d 813, 817 (2d Cir. 1996) (question of collateral estoppel within the contemplation of the issues parties agreed to arbitrate).

Thus, there is no recent or well-defined division among the circuits as to whether arbitrators may consider the question of collateral estoppel. Especially in light of *Sherrock*, the Third Circuit does not bar arbitrators from deciding that question. The only Fifth Circuit case cited, *Miller Brewing,* is over 20 years old and deals with state law. And the Eighth Circuit cases either say just the opposite (*John Morrell*) or are limited to its own facts (*Y&A Group*). As such, there is no division of authority.

B. Any Alleged Split Among Older Cases Has Been Resolved by This Court's 2002 Decision in *Howsam*.

Not only have petitioners failed to demonstrate any division of authority among the circuits, they also have not addressed this Court's more recent decision in *Howsam v. Dean Witter Reynolds*, 537 U.S. 79 (2002) which courts have relied on to hold that arbitrators can decide preclusion issues. In *Howsam*, this Court held that while the question of "substantive arbitrability" is for a court, "procedural arbitrability, i.e., whether prerequisites such as time limits, notice, laches, estoppel and other conditions precedent to an obligation to arbitrate have been met, are for the arbitrator to decide." *Id.* at 85.

For example, in *Klay v. United Healthgroup, Inc.*, 376 F.3d 1092 (11th Cir. 2004), the court held that its earlier decision, *Kelly v. Merrill Lynch, Pierce, Fenner & Smith*, 985 F.2d 1067, 1069 (11th Cir. 1993) holding

that courts, rather than arbitrators should decide preclusion issues, could no longer stand in light of *Howsam*.[5] In *Klay*, the court considered whether arbitrators could decide the preclusive effect of an earlier court ruling and held that based on *Howsam*, "arbitrators . . . are empowered, absent an agreement to the contrary, to resolve disputes over whether a particular claim may be successfully litigated anywhere at all (due to concerns such as statute of limitations, laches, justiciability, etc.), or has any substantive merits whatsoever. . . . Consequently, . . . *res judicata* was for the arbitrator to decide in the first instance." *Id.* at 1109. Again, in *Steris Corp.*, 489 F. Supp.2d at 511, the court relied on *Howsam* to conclude that the preclusive effect of a court judgment was a "procedural question" for the arbitrator to decide. On the other hand, petitioners do not cite any division between federal courts of appeals as to whether preclusion issues are, under *Howsam*, reserved for arbitrators. As such, this only reinforces that there is no split among the circuits.

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[5] The *John Hancock Mutual Life* case cited by petitioners (Pet. at 14) relied on *Kelly* as evidence of a division of authority. 151 F.3d at 137.

III. Petitioner's Theory About Arbitrators' Supposed "Professional Hubris" or Proclivity to Pursue Fees Rather Than Apply the Law, Does Not Raise an Issue of National Importance.

Petitioners also argue that this case presents an "issue with national implications." Pet. at 18. As petitioners frame it, the issue highlights the "broader struggle between judicial and arbitral systems." *Id.* at 21. In essence, petitioners maintain that arbitrators cannot be trusted to decide questions of claim or issue preclusion. According to the petitioners, that lack of trustworthiness manifests itself in two ways. First, petitioners contend that arbitrators suffer from what they call "professional hubris" because arbitrators think that they are "simply smarter, better educated or endowed with greater industry expertise than jurors" or are "less constrained by resource or time limitations and procedural niceties than judges." Pet. at 21. Petitioners cite no authority for this sweeping proposition other than a passing comment from a magazine article (Scott Atlas & Nancy Atlas, *Potential ADR Backlash*, 10 No. 4 Disp. Resol. Mag. 14, 15-16 (2004)) and *dicta* from a 24-year old district court opinion dealing with whether arbitrators can decide the preclusive effect of a labor board decision.[6] Thus,

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[6] The other authority cited by petitioners does not come close to making the point that arbitrators have too much "professional hubris" to properly decide the preclusive effect of a judgment. Pet. at 21-22; Chris Guthrie, *Misjudging*, 7 Nev. L. J. 420, 454-55 (2007) (article observes the ways that arbitration

(Continued on following page)

there is simply no support for the categorical statement that arbitrators as a whole are too prideful to decide the preclusive effect of judgments.

Next, petitioners argue that arbitrators are so driven by self-interest that they will disregard the law of *res judicata* or collateral estoppel, so they can protract proceedings and collect more fees. Pet. at 22-23. Again, petitioners offer meager support for this wholesale dismissal of arbitrators' abilities. Petitioners merely quote a comment from a law review that is itself tentative—the quote does not include the introductory phrase "It has been said . . . " Pet. at 22; Henry S. Noyes, *If You (Re)Build It, They Will Come: Contracts to Remake the Rules of Litigation in Arbitration's Image*, 30 Harv. L. J. & Pub. Pol'y 579, 587 (2007). And petitioners' citation to another law review (Mark Berger, *Arbitration and Arbitrability: Toward an Expectation Model*, 56 Baylor L. Rev. 753, 787-88 (2004)) states just the opposite; namely, that there is "no documented support" that "arbitrators will put their own interests ahead of their responsibility."

What is more, courts have demonstrated that they are comfortable with having arbitrators decide such issues and there is no widespread judicial reluctance to having them do so. *See, e.g. Klay*, 376 F.3d at

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may be a more "accurate" and appealing forum); *John Morrell*, 913 F.2d at 562 (court's reference to overturning arbitrator's award if it reflects his "own brand of industrial justice" is merely a statement of the standard of review and says nothing about arbitrators being too prone to "hubris" to follow the law.).

1109 ("*res judicata* was for the arbitrator to decide in the first instance"). For example, contrary to petitioners' claim that arbitrators are too self-possessed or self-interested to decide preclusion issues, in *Sherrock*, 2008 WL 63300 at *3, the Third Circuit concluded that the arbitrators correctly applied *res judicata* and collateral estoppel to bar relitigation of the matters already decided in court. At bottom, petitioner's argument about a "broader struggle" is little more than another version of the perennial debate about the "pros and cons" of arbitration versus litigation. It scarcely presents an issue of national importance.

IV. The Petitioners Cannot Show That The Outcome Would Be Any Different if They Received Relief in This Court.

As shown in Section I above, petitioners presented a different issue to the Ninth Circuit than they now present to this Court. Yet even assuming this Court were to reach the question now presented, they cannot show that the outcome would be any different if this Court were to hold that the issue of collateral estoppel must be decided by a court and not an arbitrator. This is so because, as this Court made plain in *Parklane Hosiery Company, Inc. v. Shore*, 439 U.S. 322 (1979), the application of offensive nonmutual collateral estoppel, as petitioners seek here, is not automatic and it always requires a weighing of a variety of factors. *Id.* at 331. No court in this case,

however, has ever weighed these factors and petitioners have not requested this Court do so here.

While petitioners do not expressly state the relief they are requesting before this Court, apparently they seek a reversal so as to send the issue of collateral estoppel back to the district court. Petitioners requested different relief from the Ninth Circuit. There, petitioners requested that the court reverse the district court's order, enter judgment in favor of petitioners, and award petitioners compensatory and punitive damages. *See* Section I.B. at 7. The Ninth Circuit rejected petitioners' request and did not conduct a fact-specific analysis as required under *Parklane Hosiery* as to whether collateral estoppel should be applied.

Like the Ninth Circuit, the district court never conducted an analysis of whether collateral estoppel applies to this case. In fact, in its 2005 Order that is the basis of this appeal, the court specifically stated: "The Court expresses no opinion on whether collateral estoppel in fact bars relitigation of issues related to the alleged 30,000 share promise. . . . The issue before the Court at this stage is not whether Plaintiffs established all of the elements of collateral estoppel . . . , but rather whether the arbitrators manifestly disregarded the law by refusing to even consider Plaintiffs' collateral estoppel argument because the *Hickcox* judgment was on appeal." Pet. App. at 45a.

Thus, if this case were remanded, the district court would be required to analyze whether collateral estoppel applies under *Parklane Hosiery*. Therefore,

the district court could reach the same result as the arbitrators on the issue of collateral estoppel and the outcome of the case would be the same. While it is not uncommon for this Court to remand cases where the outcome is uncertain, in this case, it bears mentioning that a remand only would result in additional litigation that would not necessarily change the outcome of the case.

CONCLUSION

The petition for certiorari should be denied.

Respectfully submitted,

D.R. Horton, Inc.

E. KING POOR
Counsel of Record
QUARLES & BRADY LLP
500 West Madison Street
Suite 3700
Chicago, Illinois 60611-2511
(312) 715-5000

LONNIE J. WILLIAMS, JR.
C. CHRISTINE BURNS
QUARLES & BRADY LLP
One Renaissance Square
Two North Central Avenue
Phoenix, Arizona 85004-2391
(602) 229-5200

Attorneys for Respondent

Dated: February 27, 2008

App. 1

No. 05-15737

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JULIE E. COLLINS, ROBERT B. RYAN, INDIVIDUALS,

Plaintiffs-Appellants,

vs.

D.R. HORTON, INC., A DELAWARE CORPORATION,

Defendant-Appellee.

On Appeal from the United States
District Court for the District of Arizona
Hon. Roslyn O. Silver, Presiding

OPENING BRIEF OF APPELLANTS

STEPTOE & JOHNSON UP
LAWRENCE ALLEN KATZ
BENNETT EVAN COOPER
ELIZABETH A. SCHALLOP CALL
Collier Center
201 East Washington Street, Suite 1600
Phoenix, Arizona 85004-2382
(602) 257-5200
Attorneys for Appellants Julie E. Collins
and Robert B. Ryan

* * *

App. 2

[Page 1]

STATEMENT OF JURISDICTION

This is an appeal from the final judgment of the United States District Court for the District of Arizona confirming the arbitration award in the contract and fraud action by plaintiffs-appellants Julie E. Collins and Robert B. Ryan against defendant-appellee D.R. Horton, Inc. ("DRH"). (ER.243, 244.)[1] The district court entered its judgment on March 21, 2005. (ER.244.) Collins and Ryan timely filed their notice of appeal on April 19, 2005. (ER.246.)

The district court had jurisdiction of this action under 28 U.S.C. § 1332 (2002). This Court has jurisdiction of this appeal under 28 U.S.C. § 1291 (2002).

STATEMENT OF THE ISSUE PRESENTED

Julie Collins, Robert Ryan, and Tom Hickcox were part of a management team that received, as a group, the same fraudulent promise from DRH, and they filed lawsuits alleging identical contract and fraud claims. DRH litigated and lost the first action brought by Hickcox. Collins' and Ryan's claims were then tried to arbitrators, who refused to apply collateral estoppel because DRH had appealed Hickcox's

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[1] "CR" refers to the docket number in the district court clerk's record. "ER" refers to the tab number in Appellants' Excerpts of Record. The ER numbers are the same as the CR numbers.

judgment. The district court found that the arbitrators had committed legal error in allowing DRH to relitigate the issues but held that they did not show "manifest disregard of the law" because they did not subjectively understand their error. Did the court err by failing to vacate the arbitration award?

STATEMENT OF THE CASE

A. Nature of the Appeal

This appeal arises from two parallel lawsuits for breach of contract and fraud brought in the district court by three former employees of D.R. Horton, Inc. ("DRH"), Julie Collins, Robert Ryan, and Tom Hickcox. All three had been

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Second, the preclusive effect of the judgment in *Hickcox* was not changed by DRH's appeal. As this Court has recognized, the pendency of an appeal should "in no way affect the 'firmness' of the . . . district court [decision] for purposes of issue preclusion." *Robi v. Five Platters, Inc.*, 838 F.2d 318, 327 (9th Cir. 1988); *see also Hawkins v. Risley*, 984 F.2d 321, 325 (9th Cir. 1993) (following *Robi*). Leading commentators confirm that "in federal courts . . . the preclusive effects of a lower court judgment cannot be suspended simply by taking an appeal that remains undecided." 18A Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and*

Procedure § 4433, at 71 (2d ed. 2002) ("Wright & Miller"). Indeed, that rule has been settled for over a century. *Id.* at 78-79. While "[f]ederal [sic] law governs the collateral estoppel effect of a case decided by a federal court," *Trevino v. Gates*, 99 F.3d 911, 923 (9th Cir. 1996), the law of Arizona, the locus of the dispute, similarly disregards the pendency of an appeal in applying preclusion doctrines. *See Ariz. Downs v. Superior Court*, 623 P.2d 1229, 1232 (Ariz. 1981) (adopting majority rule).

In light of the clear governing law, the arbitrators were not entitled to disregard the preclusive effect of the *Hickcox* judgment just because they were concerned about the possibility that the judgment might be upset on appeal. It is not unusual for there to be two actions in which "the second judgment has become conclusive even though it rested solely on a judgment that was later reversed." 18A Wright & Miller, *supra*, at 88-89 (collecting cases). In those cases, the rule recognized by this Court in *Robi* still applies because, "[d]espite the manifest risks of resting preclusion on a judgment that is being appealed, the alternative of retrying the common claims, defenses, or issues is even worse," i.e., "the burdens of retrial, the potential for inconsistent results, and the occasionally bizarre problems of achieving repose and finality that may arise." *Id.* at 94.

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Moreover, to the extent that the binding nature of the arbitration was an issue, DRH brought this situation on itself not only by agreeing to binding arbitration but also by moving, successfully, over Collins and Ryan's objections, to compel arbitration of their claims on the eve of trial, after two years of litigating in the district court. (*See* CR.171, 172.) Indeed, the *Hickcox* jury returned its verdict and Judge Bolton entered judgment on it shortly after Judge Silver ordered arbitration on DRH's motion. The verdict and judgment put DRH on notice of the preclusive effect that judgment would have on Collins' and Ryan's claims. In light of these circumstances and Collins and Ryan's subsequent motion for reconsideration, DRH could have waived arbitration and litigated the issues in district court, thereby recovering the option of appeal. The arbitrators' invocation of "practicality and fairness" furthered only impracticality and unfairness.

The arbitrators improperly arrogated to themselves the right to restrike the balance between preclusion and finality. No doubt a few state courts, possibly out of a similar concern for reversal on appeal, require that the appellate process be concluded before a judgment will be given preclusive effect in another proceeding. *See, e.g., Swaffield v. Universal Ecsco Corp.*, 76 Cal. Rptr. 680, 687 (Ct. App. 1969) ("the California rule is that a judgment is not final for purposes of collateral estoppel until final disposition on appeal"). The federal courts, however,

have determined that pendency of the appeal should be disregarded unless and until the judgment is actually vacated – indeed, they have done so uniformly. *See generally* 18A Wright & Miller, *supra*, § 4433, at 71. The federal courts' determination was binding on the arbitrators and, more importantly, on Judge Silver.

Indeed, the very chronology of this case suggests a textbook example of the mischief that may result from allowing preclusion to be undone by the mere pendency of an appeal and "the bizarre problems of achieving repose and finality that may arise." 18A Wright & Miller, *supra*, at 94. Upon its entry, the *Hickcox*

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framework" for the "manifest disregard" standard. Stephen L. Hayford, *Reining in the "Manifest Disregard" of the Law Standard: The Key to Restoring Order to the Law of Vacatur*, 1998 J. Disp. Resol. 117, 134, *cited in* 361 F. Supp. 2d at 1100. Quoting the article, the district court declared that "an error of law, 'no matter how obvious or outrageous a court may deem it to be, cannot alone justify vacatur,'" because the court must also make a "'two-dimensional, mens rea'-like, state of mind determination.'" 361 F. Supp. 2d at 1100 (quoting Hayford, *supra*, at 124). The author of the article admitted, however, that his proposal established a "very narrow scope" for the standard and that "[n]one of the current models for

the 'manifest disregard' of the law analysis orders the judicial inquiry in the manner described above." Hayford, *supra*, at 136. Given the numerous circuit decisions discussing the "manifest disregard" standard and its application, it is remarkable that the district court would choose to rely on an obscure legal commentary for an admittedly "very narrow" and unprecedented interpretation of the standard.

Moreover, the district court's adoption of a subjective "mens rea" requirement is completely unworkable. Proving the "state of mind" of the arbitrators – whether they "'have consciously or intentionally chosen not to apply [the law] to the facts of the case'" – would require parties to depose arbitrators after they have rendered their decisions. *Collins*, 361 F. Supp. 2d at 1100 (quoting Hayford, *supra*, at 124). Without such discovery as a check, arbitrators would quickly learn that, unless they were to declare openly their nullification of the law, they could escape any meaningful judicial scrutiny by simply omitting or obscurely stating their reasoning, regardless of how "obvious or outrageous" their departure from the law might be. The result would be rulings so cryptic that parties would lose all faith in the arbitration process, which would undercut the federal policy in favor of arbitration.

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In fact, the established precedent in this Court and elsewhere does not impose any "mens rea" standard in demonstrating manifest disregard. Indeed, in

requiring that the "disregard" be "manifest," the courts have avoided such purely subjective determinations of the arbitrator's actual state of mind. The 1961 *San Martine* case cited by the district court was one of this Court's earliest articulations of a non-statutory ground for vacatur of an arbitration award. The Court merely stated that "manifest disregard of the law must be something beyond and different from mere error in the law or failure on the part of the arbitrators to understand or apply the law." 293 F.2d at 801. The Court gave a single but non-exclusive example: "We apprehend that a manifest disregard of the law . . . might be present when arbitrators understand and correctly state the law, but proceed to disregard the same." *Id.*

Since then, however, the Court has provided further guidance as to circumstances under which an arbitration award may be deemed to be in manifest disregard of the law. In *American Postal Workers Union v. United States Postal Service*, 682 F.2d 1280 (9th Cir. 1982), for example, the Court affirmed the district court's vacatur of an arbitration award in favor of a government employee where the *undisputed facts compelled the conclusion* – contrary to that reached by the arbitrator – that the employee had participated in a strike and therefore should not be reinstated under federal law. *Id.* at 1284-85. The Court later cited its *American Postal* decision as "recogniz[ing] that an arbitration decision in manifest disregard of law *and fact* will not be upheld." *Pac.*

Reins. Mgmt. Corp. v. Ohio Reins. Corp., 935 F.2d 1019, 1025 (9th Cir. 1991) (emphasis added).

Even more recently, in *Coutee v. Barrington Capital Group*, 336 F.3d 1128 (9th Cir. 2003), the Court recognized that "*American Postal* stands for the unexceptional proposition that a federal court will not confirm an arbitration award that is *legally irreconcilable with the undisputed facts*." *Id.* at 1133. As the Court

* * *

App. 10

No. 05-15737

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JULIE E. COLLINS, ROBERT B. RYAN, INDIVIDUALS,

Plaintiffs-Appellants,

vs.

D.R. HORTON, INC., A DELAWARE CORPORATION,

Defendant-Appellee.

On Appeal from the United States
District Court for the District of Arizona
Hon. Roslyn O. Silver, Presiding

APPELLANTS' REPLY BRIEF

STEPTOE & JOHNSON UP
LAWRENCE ALLEN KATZ
BENNETT EVAN COOPER
ELIZABETH A. SCHALLOP CALL
Collier Center
201 East Washington Street, Suite 1600
Phoenix, Arizona 85004-2382
(602) 257-5200
Attorneys for Appellants Julie E. Collins and Robert B. Ryan

* * *

that burden would be carried by a finding that the policy was "explicit, well-defined, and dominant."

Furthermore, in *Coutee v. Barington Capital Group*, 336 F.3d 1128, 1133 (9th Cir. 2003), the Court held that "an arbitrator's failure to recognize undisputed, legally dispositive facts may properly be deemed a manifest disregard for the law." Again, no specific proof of the arbitrator's personal understanding and correct statement of such facts was required, because that finding would be implicit in the existence of "undisputed, legally dispositive facts." *Coutee* and the *Carpenters* cases are thus harmonious with *San Martine* and do not require direct proof of the mens rea that the district court deemed essential to finding manifest disregard.

Collins and Ryan are entitled to an order vacating the arbitration award under the criteria recognized by this Court. The Supreme Court's *Arizona* and *Montana* decisions establish that "a fundamental precept of common-law adjudication is that an issue once determined by a competent court is conclusive," 460 U.S. at 619, and this Court's Clements decision establishes that collateral estoppel reflects an important "public interest" because it helps maintain "confidence in the judicial process," 69 F.3d at 330. It is thus beyond dispute that collateral estoppel is an "explicit, well-defined and dominant policy," and when arbitrators refuse to apply that doctrine, the

courts' usual willingness to tolerate errors in an arbitral forum must give way to a greater interest.

CONCLUSION

The Court should remand this matter to the district court with instructions to enter judgment in favor of Collins and Ryan for compensatory and punitive damages consistent with those awarded in *Hickcox*.

DATED this 15th day of December, 2005.

* * *

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FILED

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OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 07-849

IN THE

Supreme Court of the United States

JULIE E. COLLINS and ROBERT B. RYAN,

Petitioners,

v.

D.R. HORTON, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY BRIEF

BENNETT EVAN COOPER
Counsel of Record
LAWRENCE ALLEN KATZ
STEPTOE & JOHNSON LLP
Collier Center
201 East Washington Street
Suite 1600
Phoenix, Arizona 85004-2382
(602) 257-5200

Attorneys for Petitioners

214622

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

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ARGUMENT

I. THE QUESTION PRESENTED WAS OFTEN AND CLEARLY RAISED BELOW.

DRH devotes more than a third of its Brief in Opposition to asserting that Collins and Ryan failed to contend, in both the district court and in the Ninth Circuit, that a court has ultimate responsibility, not limited by the "manifest disregard" standard, for determining the preclusive effect of a court judgment on a later arbitration. Before the district court and the Ninth Circuit, however, Collins and Ryan presented the issue raised by their petition in such a manner that "the lower court [was] fairly put on notice as to the substance of the issue." *Nelson v. Adams USA, Inc.*, 529 U.S. 460, 469 (2000); *see PGA Tour, Inc. v. Martin*, 532 U.S. 661, 676-78 n.27 (2001) (petitioner's question of ADA Title III coverage not precluded for failure to make the exact same argument below, since the coverage issue had generally been raised in the lower courts).

A. The Issue Was Raised Multiple Times in the District Court.

Collins and Ryan raised this issue both times it was before the district court, and the district court rejected Collins and Ryan's position. Before the arbitration, they argued to the district court that "this Court, not an arbitrator, should decide both the merits of the fraud claims themselves and the issue of collateral estoppel."

ER.220, at 2. The district court stated the issue, and its view, as follows:

> This Court must decide a matter of first impression in the Ninth Circuit: whether the collateral estoppel effect of a court-rendered judgment is to be determined by a court in a subsequent action, or by arbitrators. Plaintiffs assert that because a Federal District Court Judge rendered this Judgment, only a Federal Court may decide its collateral estoppel effects. The Court rejects this argument.

ER.228, at 7; *see also id.* at 13.

After the arbitrators refused to apply collateral estoppel, Collins and Ryan again raised the issue before the district court in their motion to vacate that part of the arbitrators' award. CR.229. The court had already allowed the arbitrators to decide the collateral estoppel issue in the first instance. Therefore, citing many of the cases later cited in the petition, Collins and Ryan urged the court to exercise "'plenary review'" and "determine the collateral estoppel effect of the *Hickcox* judgment on Plaintiffs' identical claims, and to enter judgment in Plaintiffs' favor." *Id.* at 7-8 (quotation omitted). The district court chose not to do so. Rather, it applied the usual deferential standard for *arbitrable* issues and held that the arbitrators' ruling, though erroneous, was not reversible as manifest disregard for the law. Pet. App. at 51a, 56a.

B. The Question Was Raised, Argued, and Decided in the Ninth Circuit.

DRH also argues that Collins and Ryan failed to raise the "court or arbitrator" issue in the Ninth Circuit, and it points to the "Issue Presented" section of their opening brief and other selected portions of the record. Br. Opp'n at 5-7. DRH fails to look in the right place.

In their opening brief to the Ninth Circuit, Collins and Ryan cited nearly all of the authorities later presented in their petition, again contending that courts have the "plenary" authority to determine the preclusive effect of prior judgments. They noted, "Indeed, numerous courts, expressing concern that arbitrators may decline to apply preclusion doctrines, have recognized the authority of courts to make the *ultimate determination* of whether such doctrines apply." Opening Br. at 2, 4, 11, 13, 28-29 (emphasis added).

In their reply brief, Collins and Ryan continued to argue forcefully that even though "the district court committed the issue of collateral estoppel to the arbitrators *in the first instance*," it was nevertheless "[t]he *non-delegable duty* of the federal court to preserve the effectiveness of its own prior judgment." Reply Br. at 1 (second emphasis added). Collins and Ryan devoted fully two pages to their argument that the courts must have the final say in whether their own decisions would have preclusive effect on future cases:

> The need for federal courts to review arbitral decisions on the collateral estoppel effect of prior federal court judgments is

> implicit in the existing debate over *when* in the process the courts should intervene. Some courts hold that the district court should determine the preclusive effect of its own prior judgment *before* the case is submitted to arbitration, while others hold that the arbitrators should be allowed to address the issue in the *first* instance. Nevertheless, there is a general agreement that *courts* should make the *final* determination as to the preclusive effect of a prior court judgment.

Id. at 23 (footnotes omitted).

During oral argument before the Ninth Circuit, Collins and Ryan's counsel again raised the courts' plenary authority to determine the preclusive effect of a prior judgment, free of the manifest disregard standard:

> Because it's collateral estoppel and other circuits have said that it is up to the courts, not arbitrators, ultimately to decide the collateral estoppel effect of prior federal court judgments. That is for the court to decide, not the arbitrators. And even where one lets the arbitrators take a first shot at it, if they make a mistake, whether it's manifest disregard, or simple error, the court should correct that. And numerous circuits have said that it is not ultimately an arbitrator issue, it's a court issue.

Counsel pressed this argument:

> But we think [that manifest disregard is] not the proper standard. The proper standard whether it's an issue of first impression in the circuit or not, is . . . whether you even apply the manifest disregard standard to collateral estoppel. We urge the court not to do that because this is a fundamental right, a fundamental precept.

The panel reflected its consideration of this issue when it asked DRH's attorney, "Can you respond to Mr. Cooper's argument that manifest disregard is not the standard of review here?" DRH's counsel replied that "this circuit, in my opinion, has made it clear that [manifest disregard] is the standard."

The Ninth Circuit then squarely decided the issue. It held that (i) "arbitrators are entitled to determine in the first instance whether the prerequisites for collateral estoppel are satisfied," Pet. App. at 17a (quotation omitted); (ii) that they "possess the same broad discretion possessed by district courts to determine when to apply offensive non-mutual collateral estoppel," *id.*; and (iii) that the arbitrators' decision would be review deferentially for manifest disregard, not on a plenary basis, *id.* at 21a.

That this was a considered ruling, however erroneous, is clear because the opinion in this case was really a sequel to the Ninth Circuit's 2000 opinion in *Chiron Corp. v. Ortho Diagnostic System, Inc.*, 207 F.3d 1126, 1134 (9th Cir. 2000). In *Chiron*, the court held that

an arbitrator could determine the preclusive effect of another arbitrator's prior ruling. After reviewing the rulings by other circuits – including many of the cases cited in the petition – it specifically reserved whether an arbitrator could also make that determination when the prior ruling issued from a court. The court acknowledged "the presumption that the court issuing the original decision is best equipped to determine . . . what is or is not precluded by that decision." *Id.* In this case, the Ninth Circuit answered that reserved question by backing away from the "presumption." The court could not have expressed its view on "court versus arbitrator" in any clearer way. The issue is squarely presented for this Court.

II. THERE IS A WELL-DEFINED SPLIT AMONG THE CIRCUITS ON THE QUESTION PRESENTED.

A. DRH Fails to Reconcile Obvious Differences Among Circuits.

DRH argues that there is no split among the circuits on whether a court or an arbitrator should determine the preclusive effect of a prior court judgment. Br. Opp'n at 9. Challenging Collins and Ryan's statement that, in contrast to the Ninth Circuit, the Third, Fifth and Eighth Circuits have held that "courts' consideration of preclusion issues is plenary, not limited by the usual manifest disregard standard," Pet. at 14, DRH contends that those circuits are "far from holding that an arbitrator can never decide the issue of collateral estoppel," Br. Opp'n at 10. DRH further argues that Collins and Ryan overlook the difference between

res judicata and collateral estoppel. *Id.* at 12-13. Finally, DRH maintains that this Court's decision in *Howsam v. Dean Witter Reynolds*, 537 U.S. 79 (2002), resolved any alleged split among the circuits on the question presented. Br. Opp'n at 14-15.

First, Collins and Ryan have *not* argued that an arbitrator can "never decide" the preclusive effect of a prior court judgment in the first instance. Rather, it has always been their position that the court must exercise its plenary authority to be the *ultimate* decision maker on this issue, if and when called upon, either before or after arbitration. Pet. at 1, 14. In many instances, the arbitration will take place before a court ever looks at the case. The Third Circuit recognized that possibility in *Telephone Workers Union v. New Jersey Bell Telephone Co.*, 584 F.2d 31 (3d Cir. 1978), one of the cases in conflict with the Ninth Circuit's ruling:

> When a federal court is presented with the contention that a prior federal judgment determined issues now sought to be relitigated in an arbitral forum it must first determine the effect of the judgment. This is so whether the question arises in an action to compel arbitration, or, as here, in an action to enforce a disputed award.

Id. at 33 (internal citations omitted). DRH contends that *Telephone Workers* is somehow irrelevant because it is a thirty-year old case and was decided on a motion to enforce arbitration rather than a motion to compel.

Br. Opp'n at 10. However, *Telephone Workers* has not been overruled, and it is still good law in the Third Circuit.[1]

DRH also argues that the Third Circuit's opinion in *John Hancock Mut. Life In. Co. v. Olick*, 151 F.3d 132 (3d Cir. 1998), does not reflect a conflict with the Ninth Circuit because the preclusive effect of a prior court decision on an arbitration was being reviewed under the doctrine of res judicata rather than collateral estoppel. Br. Opp'n at 10. But these are sister doctrines[2] and, in recognizing a conflict among circuits as to whether the existence of a prior judgment would require the district

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[1] DRH tries to cast doubt on the continued validity of *Telephone Workers* by citing the Third Circuit's recent unpublished decision in *Sherrock Brothers, Inc. v. DaimlerChrysler Motors Co.*, 2008 WL 63300 (3d Cir. 2008). Br. Opp'n at 11. But *Sherrock Brothers* is clearly off target: the arbitration panel decided the effect of a prior decision of a state board, not a prior court judgment as DRH claims. In addition, the court in *Sherrock Brothers* found that the arbitrator had applied correct legal principles and did not opine on what the result would have been had the arbitrators ruled incorrectly. DRH also cites *Steris Corp. v. International Union*, 489 F. Supp. 2d 501 (W.D. Pa. 2007), but that case concerned the preclusive effect of a prior *arbitration* decision. Br. Opp'n at 11.

[2] "[C]ollateral estoppel, like the related doctrine of res judicata, has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 (1979). "Application of both doctrines is central to the purpose for which civil courts have been established, the conclusive resolution of disputes within their jurisdiction." *Montana v. United States*, 440 U.S. 147, 153 (1979).

court to enjoin a subsequent arbitration, the Third Circuit cited cases dealing with both res judicata and collateral estoppel. 151 F.3d at 137-38. Here, the application of collateral estoppel would have had the same effect as res judicata, because it would have disposed of the entire claim, not just an issue.

DRH also argues that the Fifth Circuit case cited by Collins and Ryan, *Miller Brewing Co. v. Fort Worth Distributing Co.*, 781 F.2d 494 (5th Cir. 1986), does not demonstrate a split among the circuits on federal law because it deals with Texas law. Br. Opp'n at 11. However, while the Fifth Circuit did look at Texas law in *Miller Brewing*, it also addressed the issue under the Federal Arbitration Act, holding:

> The Arbitration Act contemplates that awards made pursuant to arbitration will be confirmed in the federal courts. 9 U.S.C. § 9. Since an arbitration award involves the entry of judgment by a court, parties should be barred from seeking relief from arbitration panels when, under the doctrine of res judicata, they would be barred from seeking relief in the courts.

781 F.2d at 499. Thus, DRH's argument that this case has no bearing on a division among the circuits and state courts[3] on federal law is without merit.

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[3] *See also Johnson v. California*, 545 U.S. 162, 164 (2005) (granting certiorari to settle conflict between California Supreme Court and Ninth Circuit regarding application of federal law); (Cont'd)

Lastly, DRH attacks Petitioners' reliance on the Eighth Circuit to evidence a circuit split. DRH argues that the holding of *In re Y & A Securities Litigation*, 38 F.3d 380 (8th Cir. 1994) – that courts have the "power to defend their judgments as res judicata" – was limited to a consent decree. Br. Opp'n at 12. However, DRH's use of the term "consent decree" exceeds poetic license because, in actuality, the court used only the term "consent judgment," indicating that it was treating the ruling below like any other judgment. Furthermore, the majority broadly stated that, "[n]o matter what, courts have the power to defend their judgments as *res judicata*, including the power to enjoin or stay subsequent arbitrations." 38 F.3d at 382. The court explained that "[t]he district court, and not the arbitration panel, is the best interpreter of its own judgment." *Id.* at 383. DRH points out that a concurring judge expressed his own belief in the "limited" scope of the opinion, but DRH unfairly omitted the judge's next statement: "I would be most reluctant to say that a court cannot enforce its own pre-existing injunctive order, notwithstanding subsequent invocation of the arbitration process by one of the parties to the case that resulted in the injunction." *Id.* at 384-85.

DRH next argues that *John Morrell & Co v. Local Union 304A, UFCW*, 913 F.2d 544 (8th Cir. 1990), is not in conflict with the Ninth Circuit because it held that

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(Cont'd)
United States v. Estate of Romani, 523 U.S. 517, 521 (1998) (granting certiorari to settle conflict between Pennsylvania Supreme Court and federal court of appeals regarding interpretation of federal statute).

arbitrators can decide *in the first instance* whether a prior court judgment has preclusive effect. Br. Opp'n at 12. Actually, in their petition, Collins and Ryan cited *John Morrell* for the *same* proposition. Pet. at 14. Significantly, in *John Morrell*, the Eighth Circuit approved the district court's exercise of its plenary power to *overturn* the arbitrators' erroneous application of collateral estoppel – a power that the Ninth Circuit refused to recognize in the present case. The Eighth Circuit never mentioned the term "manifest disregard of the law" in ruling that "the arbitrator was barred from reconsidering the issue decided in the prior judicial proceeding." 913 F.2d at 562. Thus, *John Morrell* clearly conflicts with the Ninth Circuit's dependency on the manifest disregard standard.

B. *Howsam* Cannot Be Expanded To Cover The Question Presented Here.

DRH argues that this Court's decision in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002), is dispositive because "courts have relied on [*Howsam*] to hold that arbitrators can decide preclusion issues." Br. Opp'n at 14. DRH misconstrues and overplays the Court's holding in *Howsam*, where the Court decided that NASD arbitrators should interpret and apply a NASD rule. 537 U.S. at 81. But the Court's reasoning actually supports Collins and Ryan's position: NASD arbitrators are "more expert about the meaning of their own rule [and] are comparatively better able to interpret and to apply it." *Id.* at 80. This Court concluded: "And for the law to assume an expectation that aligns (1) decisionmaker with (2) comparative expertise will help better to secure a fair and expeditious resolution of

the underlying controversy-a goal of arbitration systems and judicial system alike." *Id.* By this reasoning, a court should have the final authority to determine the collateral estoppel effect of its own judgment, regardless of whether one defines collateral estoppel as procedural or substantive.[4]

C. Collins And Ryan Are Not Required To Show That The Outcome Would Be Different.

DRH argues against granting review because it believes that Collins and Ryan cannot show that the outcome would be any different if they received the relief requested. Br. Opp'n at 18. DRH has not cited any authority for this dubious proposition. *See Riggins v. Nevada*, 504 U.S. 127, 137 (1992) (defendant not required to show that outcome would have been different absent the error, only the possibility that the defense was impaired by the error). Certainly the outcome would be different on the specific issue decided by the arbitrators, i.e., whether the pending appeal deprived the *Hickcox* judgment of preclusive effect. Indeed, there is a strong likelihood that Collins and Ryan *would* prevail on collateral estoppel as a whole. The arbitrators themselves conceded that the argument for collateral estoppel "might be compelling if this were an appealable proceeding in a court of law." ER.229, Ex. G, at 1. Moreover, DRH has not shown that any of the factors specified in *Parklane Hosiery Co. v. Shore*, 439 U.S. 322 (1979), for rejecting offensive non-mutual collateral estoppel apply here.

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[4] DRH relies on an Eleventh Circuit case, *Klay v. United Healthgroup, Inc.*, 376 F.3d 1092 (2004), to support its labored application of *Howsam*. But Collins and Ryan cited *Klay* as consistent with the Ninth Circuit, but not other circuits. Pet. at 13.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

BENNETT EVAN COOPER
Counsel of Record
LAWRENCE ALLEN KATZ
STEPTOE & JOHNSON LLP
Collier Center
201 East Washington Street
Suite 1600
Phoenix, Arizona 85004-2382
(602) 257-5200

Attorneys for Petitioners